83-737

No._____

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IN THE

# Supreme Court of the United States

October Term, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE AND TELEGRAPH COMPANY, *et al.*,

*Appellees.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

## JURISDICTIONAL STATEMENT

JANICE E. KERR*
J. CALVIN SIMPSON
GRETCHEN DUMAS
MARK FOGELMAN
5066 State Building
San Francisco, California 94102
(415) 557-0470
*Attorneys for Appellants*

*Counsel of Record*

Batavia Times Publishing Co.
Batavia, N.Y. (716) 344-2000

## Questions Presented

1. Whether the District Court violated the provisions or principles of the Modification of Final Judgment ("MFJ") or abused its discretion in approving the plan of reorganization ("POR") without requiring that assets of the Bell Operating Companies ("BOCs") in Account 232 relating to station handling and/or complex intrasystem wiring be assigned to American Telephone and Telegraph Company ("AT&T") as constituting, or as "relating to the provision of," customer premises equipment ("CPE").

2. Whether the District Court violated the provisions or principles of the MFJ or abused its discretion in approving the POR without requiring that the average cost of the long-term funded debt retained by The Pacific Telephone and Telegraph Company ("Pacific") at the time of the divestiture be representative of the average cost of such consolidated debt held by AT&T, its affiliates and the BOCs.

## Parties Below

In addition to the United States, AT&T, Western Electric Company, Inc. and Bell Laboratories, Inc., the following parties were admitted as intervenors in the District Court: *Ad Hoc* Telecommunications Users Committee; American Newspaper Publishers Association; American Petroleum Institute; American Satellite Company; Associated Telephone Answering Exchanges, Inc.; Association of American Railroads; Association of Data Communications Users; Association of Data Processing Service Organizations; Audichron Company; Black Citizens for a Fair Media; California Hispanics; Citizens Utilities Company; Communication Commission of the National Council of the Churches of Christ in the USA; Communications Workers of America; Compuserve, Inc.; Computer and Business Equipment Manufacturers Association; Computer and Communications Industry Association; Congress Watch; Continental Telecom, Inc.; D/FW Signal, Inc.; Education and Cultivation Division of the General Board of Global Ministries of the United Methodist Church; Federal Communications Commission; General Dynamics Communications Co.; General Telephone & Electronics Corp.; Independent Data Communications Manufacturers Association; Independent Telecommunications Suppliers' Council; International Telephone and Telegraph Corp.; Jack Faucett Associates, Inc., *et al.*; Leghorn Telepublishing Co.; MCI Communications Corp.; Mobile Marine Radio, Inc.; National Association for the Advancement of Colored People; National Association for Better Broadcasting; National Association of Broadcasters; National Association of Regulatory Utility Commissioners; National Association of State Utility Consumer Advocates; National Cable Television Association; National Catholic Broadcasters Association; National Citizens Committee for Broadcasting; National Latino Media Coalition; National Newspaper Association; North American Telephone Association; Northeastern

Telephone Co.; Office of Communication of the United Church of Christ; Reformed Church in America; Rogers Radio Communication Services, Inc.; Rural Telephone Coalition; San/Bar Corp.; Satellite Business Systems; Sonitrol Distributors Council, Inc.; Southern Pacific Communications Company; Sperry Corporation; Stromberg-Carlson Corp.; Tandy Corporation; Telocator Network of America; U.S. Telephone Communications, Inc.; United States Independent Telephone Association; United States Telecommunications Suppliers Association; United Telecommunications, Inc.; Utilities Telecommunications Council; Warner Amex Cable Communications, Inc.; Western Union Telegraph Co.; Westinghouse Broadcasting and Cable, Inc.; Alarm Industry Telecommunications Committee; States of Arizona, California, Colorado, Delaware, Illinois, Maine, Maryland, Michigan, Missouri, New Hampshire, New Mexico, New York, North Carolina, Oregon, Pennsylvania, Tennessee, Virginia, Wisconsin; Alabama Public Service Commission; Arkansas Public Service Commission; California Public Utilities Commission; District of Columbia Public Service Commission; Florida Public Service Commission; Idaho Public Utilities Commission; Kentucky Public Commission; Michigan Public Service Commission; Missouri Public Service Commission; Montana Public Service Commission; Nebraska Service Utilities Commission; Nevada Public Service Commission; New York Public Service Commission; South Dakota Public Utilities Commission; Utah Public Service Commission; Public Service Commission of West Virginia; Wisconsin Public Service Commission; Wyoming Public Service Commission; Iowa Commerce Commission; Kansas Corporation Commission; New Mexico Corporation Commission; Ohio Consumers Counsel; Oklahoma Corporation Commission; Virginia State Corporation Commission; Washington Utilities & Transportation Commission; City of Cincinnati; City of New York. (Appendix to Jurisdictional Statement (App.) at 191-194.)

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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## JURISDICTIONAL STATEMENT

Appellants, the People of the State of California and the Public Utilities Commission of the State of California ("CPUC"), respectfully request that the Court note probable jurisdiction of their appeal from the District Court's memorandum and order of August 5, 1983, approving American Telephone and Telegraph

Company's ("AT&T's") proposed plan of reorganization ("POR"), as amended by AT&T and as further modified by the District Court's opinion of July 8, 1983, and memorandum of July 28, 1983. The appeal has been certified to this Court by the District Court pursuant to the Expediting Act, 15 U.S.C. §29(b).

## Opinions Below

The opinion of the District Court filed August 11, 1982 (App. at 1-172), and the Modification of Final Judgment ("MFJ") filed August 24, 1982 (App. at 173-190), are officially reported as *United States v. AT&T*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd. mem. sub nom. Maryland v. United States*, ____U.S.____, 75 L. Ed. 2d 472, 103 S. Ct. 1240 (1983).

The District Court's opinion of July 8, 1983 (App. at 195-330), not yet officially reported, is published at Trade Reg. Rep. (CCH), Rpt. No. 604 (extra ed. July 19, 1983). The District Court's memorandum of July 28, 1983 (App. at 331-340) is neither officially nor unofficially reported. The District Court's memorandum and order of August 5, 1983 (App. at 341-350), not yet officially reported, are published at 1983-2 Trade Cas. (CCH) ¶65,536. The District Court's order of September 7, 1983 (App. at 351-354), not yet officially reported, is published at 1983-2 Trade Cas. (CCH) ¶65,596.

## Jurisdiction

In this civil antitrust suit brought by the United States against AT&T and its affiliates under the Sherman Act, 15 U.S.C. §§1-4,[1] the District Court's MFJ filed August 24, 1982, has been affirmed by this Court. (*United States v. AT&T*, 552 F. Supp. 131, 226-234 (D.D.C. 1982), *aff'd. mem. sub nom. Maryland v. United States*, ___U.S.___, 75 L. Ed. 2d 472, 103 S. Ct. 1240 (1983).)

After AT&T's submission of its proposed POR as required by the MFJ, the District Court held public comment proceedings in accordance with the Tunney Act, 15 U.S.C. §16, in order to ascertain whether the POR was consistent with the MFJ as well as the public interest. In ruling on the comments submitted by appellants and others, the District Court rejected appellants' claims raised herein and, by its order of August 5, 1983, approved the POR, as amended by AT&T and as further modified by the District Court's rulings of July 8, 1983, and July 28, 1983. The District Court's order of August 5, 1983, approving the POR, is a final order for purposes of appeal.[2]

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[1] The complaint in the primary suit engendering this appeal, *United States v. Western Electric Company, Inc.* (Civil Action No. 82-0192 (D.D.C.), formerly Civil Action No. 17-49 (D.N.J.)), alleged violation of 15 U.S.C. §§1-3. The complaint in *United States v. American Telephone and Telegraph Company* (Civil Action No. 74-1698 (D.D.C.)) alleged violations of 15 U.S.C. §2. Federal jurisdiction in both cases rests on 15 U.S.C. §4 and 28 U.S.C. §1337.

[2] *See Brown Shoe Co. v. United States*, 370 U.S. 294, 310 n.16 (1962), and cases there cited.

On August 10, 1983, appellants filed a timely notice of appeal,[3] and on September 7, 1983, the District Court filed an order granting the motion of the Department of Justice for certification of this and any subsequent appeals directly to this Court pursuant to the Expediting Act, 15 U.S.C. §29(b).

Federal appellate jurisdiction is predicated on 28 U.S.C §§1291 and 2107. (*See* 15 U.S.C. §29(a).) Jurisdiction for direct appeal to this Court is conferred by 15 U.S.C. §29(b).

## Statutory Provisions

The text of 15 U.S.C. §§16 and 29 is set forth in the Appendix. (App. at 359-364.)

## Statement of the Case

On February 28, 1983, this Court affirmed the MFJ.[4] (*Maryland v. United States*, ____U.S.____, 75 L. Ed. 2d 472, 103 S. Ct. 1240 (1983).)

The MFJ (also referred to as "the decree") requires the retention by AT&T of "all facilities, personnel and books of account . . . relating to . . . the provision of customer premises equipment to the public." (MFJ, §§I(A)(2), I(A)(4); App. at 174-175.) The decree defines CPE as "equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications," not including "equipment used to multiplex, maintain, or terminate access lines." (MFJ, §IV(E); App. at 177.)

[3] The District Court's order of August 26, 1982, admitted appellants as intervenors below (App. at 191-194) and expressly conferred on appellants the right to appeal the District Court's decision concerning the POR (App. at 194).

[4] For a history of this litigation prior to the District Court's approval of the MFJ, *see* App. at 3-25.

The MFJ also provides that, at the time of reorganization, "the quality of the debt [of the separated BOCs] shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time." (MFJ, §VIII(H); App. at 184-185.)

In declaring its conditional approval of the decree, the District Court addressed the concern "that AT&T might manipulate the actual division of assets and liabilities to the detriment of the Operating Companies." (App. at 133.) It concluded that there were safeguards to protect against such abuse by AT&T, including *inter alia* the following: (1) the decree's requirement that assets be divided according to function or, where an asset serves functions relating to services to be rendered by both AT&T and the BOCs, according to its predominant use (App. at 134-136); (2) the requirement that AT&T leave with each BOC debt issues reflecting terms and conditions comparable to those of the consolidated debt held by the Bell System as a whole (App. at 136-137); and (3) the requirement that the POR not be implemented until its approval by the District Court as being consistent with the provisions and principles of the decree (App. at 156) as well as the public interest (App. at 159).

However, AT&T's plan of reorganization stated that the entire Account 232, which in large part records investments in (1) station handling, the labor costs incurred in the transportation, installation and delivery of customer premises equipment such as telephones, private branch exchanges ("PBXs") and key telephone equipment, and (2) complex intrasystem wiring used to connect on-premises business-type telecommunications apparatus and material and labor costs incurred in the

installation of such inside wiring, "does not contain customer premises equipment and, therefore, will remain with the BOCs" (POR, §I(A)(2)(a)(v), at 86). In addition, despite the MFJ's requirement that "the quality of the debt [of the separated BOCs] shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs" (MFJ, §VIII(H); App. at 184-185), the POR proposed that the cost of funded debt for each of the divested BOCs would be approximately the same, *except for Pacific Telephone*, which would be left with a substantially higher average cost of funded debt than the other six regional BOCs and the Bell System as a whole (POR, §I(B)(4), at 193-195).

Appellants vigorously opposed these provisions of the POR in their initial comments submitted to the District Court, contending that the MFJ and the public interest required (1) that the portion of Account 232 pertaining to complex intrasystem wiring and station handling costs be assigned to AT&T rather than the BOCs,[5] and (2) that Pacific, like the other BOCs, be left with a cost of funded debt in line with the average cost of debt of the Bell System as a whole. (Prelim. Comments, CPUC, at 23-31; Further Comments, CPUC, at 12-25, 46-48.) AT&T and the Department of Justice filed written opposition to these claims (AT&T Response, at 149-169, 276-305; DOJ Response, at 84-91, 117-122), and appellants replied (Reply Comments, CPUC, at 7-13, 16-26).

[5] While appellants raised the station handling issue in a general manner by including it in their Account 232 complex intrasystem wire discussion and numerical estimates in the court below (*see* note 7, *infra*), the New York Department of Public Service and other parties raised it as a separate issue. (Comments, N.Y. Dept. Pub. Serv. at 10-11; Comments, Computer and Business Equipment Manufacturers Association, at 16-17; Reply Comments, Independent Data Communications Manufacturers Association, at 31-33.)

The District Court's decision filed July 8, 1983, conditionally approving the POR (App. at 197), purports to reject appellants' cost-of-debt claim in a footnote (App. at 221-222 n.64) and fails to address the complex intrasystem wiring and station handling claims. The District Court's memorandum of July 28, 1983, requiring further modification of the POR, makes passing reference to the inside wiring claim, again in a footnote. (App. at 339 n.18.) The District Court's memorandum filed August 5, 1983, approving the POR, refers briefly to the general inside wiring and station handling claims but fails to address specifically the complex intrasystem wiring claim. (App. at 343-344.)

On August 10, 1983, appellants filed their notice of appeal herein (App. at 355-356).

On August 25, 1983, without appellants' support or participation, the Department of Justice moved for certification of this and any subsequently filed appeals directly to this Court pursuant to 15 U.S.C. §29(b). (*See* App. at 351-352.) On August 26, 1983, AT&T filed a response in support of the motion (*see* App. at 352), and on September 7, 1983, the District Court granted the motion (App. at 354).

This appeal follows.

## The Questions are Substantial

### I. Introduction

This appeal does not seek to halt the AT&T divestiture, presently scheduled to occur on January 1, 1984. No stay has been sought nor is one desired.

Instead, should appellants prevail on the merits of their claims, appropriate relief would consist of this Court's ordering the District Court, in accordance with that court's continuing jurisdiction to enforce the MFJ, to take all steps necessary to ensure (1) that station handling and complex intrasystem wiring costs reflected in Account 232 be assigned to AT&T, rather than the BOCs, and (2) that the Pacific Regional BOC be left with a portfolio of long-term debt with an average cost of debt in line with that of AT&T, its affiliates and the BOCs at the time of divestiture.[6]

The financial stakes in this appeal are staggering. It is estimated that the complex inside wiring claim alone involves net investment of approximately $3 billion nationwide and $332 million[7] for Pacific Telephone, appellants' regional BOC. It is further estimated that the station handling claim alone involves a net investment of roughly $2.3 billion nationwide and a net investment for Pacific Telephone as of December 31, 1982, of approximately $260 million.[8] The assignment of station

[6] Such relief can presumably be accomplished by the District Court's ordering or voiding conveyances, ordering reconveyances or ordering the payment of money, where appropriate.

[7] Appellants in their comments below used the figure $474 million to describe net investment for the complex inside wiring subaccount for Pacific Telephone. This included approximately $142 million of station handling costs for complex telecommunications systems.

[8] Pacific Telephone's accounting system, for one, permits disaggregation of Account 232 by telephone product group information. (*See* Pacific Telephone Vertical Embedded Analysis Reporting System.)

handling and intrasystem wiring to AT&T, rather than to the BOCs, would reduce BOC rate bases by those amounts. It would thus mean at least a $1.5 billion reduction in 1984 BOC revenue requirements nationally and a corresponding $240 million reduction in Pacific's 1984 revenue needs—reductions which would significantly mitigate anticipated increases in basic monthly rates.

Such figures, though enormous, should not be surprising. After all, this case involves what the District Court has termed "the largest corporate reorganization in history." (App. at 353.)

Appellants' claims raise the serious potential that AT&T's plan of reorganization effects a distribution of assets contrary to the provisions and principles of the decree as well as the public interest.[9] If, as appellants contend, AT&T's POR improperly grants AT&T undue competitive advantage in its newly deregulated markets at the expense of the BOCs and, ultimately, the ratepaying public who must bear the cost of the BOCs' disadvantage, such a result must not go unredressed. But that determination can only properly be made after the issues have been clearly focused by full briefing on the merits and oral argument.

With little or no analysis, the District Court has rejected appellants' claims, which involve billions of dollars and affect millions of people. The only meaningful check on the District Court's action is effective review by at least one appellate tribunal. In light of the

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[9] It is notable that both AT&T and the Department of Justice resisted the District Court's attempt to subject the POR, or implementation, phase of the proceedings below to the public interest review authorized by the Tunney Act, 15 U.S.C. §16 (App. at 359-363). The District Court forcefully rejected such arguments (App. at 149-156).

enormous stakes involved in this case and the serious possibility that the public interest has been compromised, appellants' claims warrant this Court's close scrutiny and its plenary consideration.

## II. Account 232

The FCC's Uniform System of Accounts for Telephone Companies provides for an asset account referred to as Account 232 which reflects investment in a variety of functions related to the bringing of telecommunications services onto the customer's premises. (*See generally Amendment of Uniform System of Accounts*, 85 F.C.C. 2d 818, 823-828 (1981).)[10] Consolidated investment reflected in AT&T's Account 232, amounting to approximately $15 billion,[11] includes *inter alia* the following elements: (1) *station handling*, or labor costs incurred in the delivery and installation of telephones, certain types of private branch exchanges ("PBXs") and key system apparatus on the premises of residential and business customers, and (2) *complex intrasystem wiring*, or material and labor costs incurred in the installation of wiring on the business customer's premises which connects the PBX, key telephone equipment, telephone

[10] In the past, Account 232 assets have not been recovered from the customer by up-front charges at the time of installation of a telecommunications system but instead have been capitalized. This capitalization policy allowed a customer to be connected to the phone system at minimal cost, a policy that enabled AT&T to greatly expand its customer base. Two years ago the FCC, sensitive to competitive concerns in the CPE market raised by AT&T and other vendors, ordered that all future inside wiring and station handling costs be expensed and charged to the cost-causitive customer. The previously capitalized costs were ordered to be recovered over a ten-year period with a prescribed amortization schedule. (*Amendment of Uniform System of Accounts, supra*, 85 F.C.C.2d at 823-828.)

[11] *See* Form 10K, Annual Rpt. of AT&T to SEC—Fiscal 1981, at 22.

instruments, and other components together to form the customer's telecommunications system.[12]

The MFJ provides that AT&T retain "all facilities, personnel and books of account ... relating to ... the provision of customer premises equipment to the public." (MFJ, §§I(A)(2), I(A)(4); App. at 174-175.) The decree defines CPE as "equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications." (MFJ, §IV(E); App. at 177.)

Consistent with these provisions, AT&T's plan of reorganization deems all PBXs, key system apparatus and telephone instruments to be CPE and assigns them to AT&T. (POR, §I(A)(2), at 78-82.) However, the POR goes on to assign the entirety of Account 232, including station handling and complex intrasystem wiring costs, to the BOCs. (POR, §I(A)(2)(a)(v), at 86.)

Appellants contend that the assignment of the station handling and complex intrasystem wiring costs reflected in Account 232 to the BOCs, rather than to AT&T, violates the provisions and principles of the MFJ as well as the public interest. Appellants request that this Court modify the POR to secure its compliance with the MFJ or order the District Court to do so.

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[12] Account 232 also includes investment in the installation of (1) simple inside wiring for residential and small business telephones and related installation costs and (2) drop and block wire, associated protectors and related installation costs.

For purposes of this appeal, it is important to distinguish between the two types of inside wiring, each of which is designated by the nature of the customer premises installation, *i.e.*, *simple* wiring and *complex intrasystem* wiring. The former is typically found in a residential setting, between the protector block near the outside of the residence and the jack to which the home telephone instrument is connected. The latter, typically found in business installations, connects the PBX, key telephone equipment, telephone instruments, and other components together to form the customer's complex on-premises telecommunications system.

### A. Station Handling

By assigning the $2.3 billion in station handling costs reflected in Account 232 to the BOCs, the POR enables AT&T to obtain already-installed telephones, PBXs and key system apparatus at a cost which covers only the equipment and to impose on the BOCs the costs actually incurred in the delivery, installation and testing of that equipment.[13] The arrangement flatly violates the decree's requirement that AT&T retain all "books of account ... *relating to ... the provision of* customer premises equipment to the public." (App. at 174-175.) It contravenes generally accepted accounting principles which include the costs of delivery and installation in the cost of the machinery installed. (Reply Comments, CPUC, at 21-22.) It also violates the decree's principle that assets are to be divided according to function (App. at 134-6); station handling has everything to do with AT&T's CPE functions and nothing to do with the BOC's exchange telecommunications and exchange access functions.

Indeed, AT&T acknowledges that conceptually station handling investments may be considered CPE but argues that its inability to separate out the different elements of Account 232 renders its retention of such assets impracticable. (AT&T Response, at 154-155.) The Department of Justice supinely accepts this claim. (DOJ Response, at 91 n.*.) The District Court also accepts AT&T's argument, while recognizing that "a theoretical

[13] A portion of station handling costs relates to installation of CPE which will, at divestiture, have been sold to BOC customers pursuant to sales programs authorized by state regulatory agencies. Inasmuch as these CPE assets will not be assigned to AT&T, appellants propose that this portion of station handling costs also not be assigned to AT&T.

case could be made that, since under the plan embedded CPE is being assigned to AT&T, so should this portion of Account 232." (App. at 344.)

However, in reaching its conclusion the District Court completely ignores the comments of New York[14] and California,[15] which together regulate approximately 20 percent of the pre-divestiture Bell System, to the effect that the BOCs in California and New York had already separated out the various elements of Account 232 and that other states would not find it difficult to do the same. What makes AT&T's position particularly unconscionable is that AT&T was undoubtedly aware that its two largest operating company subsidiaries had broken out the elements of Account 232 when it asserted that this was impossible. Even more troubling is why the Department of Justice and the District Court, faced with the comments of California and New York, never even questioned AT&T on this important factual dispute between the company and the regulatory agencies of the two largest states.

AT&T surmises that the BOCs will be allowed by state regulatory agencies to recover this multi-billion dollar investment by increasing local telephone rates charged to ratepayers who may not be customers of AT&T's CPE operations.[16] Such a scenario is neither fair to the ratepaying public nor consistent with the MFJ.

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[14] Comments, N.Y. Dept. Pub. Serv., at 11.

[15] Further Comments, CPUC, at 24; Reply Comments, CPUC, at 26.

[16] Affidavit of Zane F. Barnes, President of Southwestern Bell Telephone Company, December 13, 1982, pgs. 3-4. Affidavit of Wallace R. Bann, designated Chief Executive Officer of the Southwest Regional Holding Company, dated December 14, 1982, at 2-3.) Supplemental Statement of Donald E. Guinn, Chairman of the Board and Chief Executive Officer of Pacific Telephone dated January 13, 1983, at 3.

### B. Complex Intrasystem Wiring

PBXs and key telephone equipment are essentially "switchboards" that route calls once they have entered a customer's place of business. Complex intrasystem wiring connects a PBX or key system machine, telephone instruments, and other components to form a complex telecommunications system on the customer's premises.

As above noted, AT&T has assigned to itself substantially all PBXs, key system machines and telephone instruments as CPE. (POR, §I(A)(2), at 78-82.) Nevertheless, it has assigned all complex intrasystem wiring, which joins the components of a customer's complex business CPE system, to the BOCs. (POR, §I(A)(2)(a)(v), at 86.)

The assignment of complex intrasystem wiring to the BOCs flatly violates the provisions and principles of the MFJ. First, the definition of CPE contained in the MFJ clearly embraces complex inside wiring. That definition is "equipment employed on the premises of a person . . . to . . . route . . . telecommunications." (MFJ, §IV(E); App. at 177.)

Second, even if such inside wiring were not deemed CPE, it most certainly constitutes "facilities, personnel, and books of account . . . *relating to* . . . *the provision of* customer premises equipment to the public." (MFJ, §I(A)(2); App. at 174-175.)

In the past, CPUC has recognized the integrated nature of complex on-premises telecommunications systems by including an intrasystem wiring charge in most Pacific Telephone tariffs for PBX and key system apparatus. Such wiring charges recover a substantial portion of the annual carrying costs of Pacific's

investment in complex intrasystem wiring. When complex CPE systems are transferred to AT&T upon divestiture it is only logical that the entire group of assets be kept as a unit. (*See* Kieso & Weygandt, Intermediate Accounting (1974), at 437.) Failure to do so will permit AT&T either to reap excessive profits by maintaining CPE rental charges at their present levels, or to undercut its competitors by reducing such charges to reflect the fact that it no longer need recover investments in complex intrasystem wiring.

AT&T's assignment of such wiring to the BOCs is unfair to local ratepayers and imposes an unreasonable burden on the BOCs. As noted above, investment in complex intrasystem wiring is now being recovered in part through equipment rates to business customers. If business customers are to continue to pay for this wiring, it should be transferred to AT&T, with the expectation that AT&T will charge those customers for the wiring as part of the complex CPE rate.

Beyond these considerations, assigning assets related to complex intrasystem wiring and associated installation costs to the BOCs, rather than to AT&T, violates the MFJ's central principle that assets be divided according to function. (App. at 134-136.) The function of complex intrasystem wiring is inextricably entwined with the function of the complex CPE assigned to AT&T. Conversely, complex intrasystem wiring has little or no relationship to the exchange functions assigned to the BOCs. The complex intrasystem wiring in Account 232 is only found *beyond* the PBX or key system unit, which is itself CPE to be transferred to AT&T; complex intrasystem wiring is in no way an extension of the local exchange outside the customer's premises.

In addition, the retention of intrasystem wiring by the BOCs presents significant potential operational problems. According to testimony filed by Pacific Telephone in its current rate case before CPUC,[17] installation and maintenance, sales, engineering, and other support personnel who are now assigned to install and service complex CPE, including intrasystem wiring, will accompany such equipment when it is transferred to AT&T. Such personnel will also be performing installation and maintenance for AT&T's new complex CPE systems, including intrasystem wiring. If intrasystem wiring is not transferred to AT&T at the same time as the associated complex apparatus and the personnel who install and maintain it, the BOCs will either have to contract with AT&T to have installation and maintenance performed on existing intrasystem wiring or will have to set up a new business installation and maintenance force to work on such equipment.

Moreover, it appears that AT&T, contrary to the terms of the decree (MFJ, §I(A)(2), at 174-175), has selectively retained all facilities and personnel relating to the provision of CPE but not all the associated investments on the books of account.

Complex on-premises telecommunications systems are a package; one company should own, offer for sale, install and recover rates for that package, and that is

[17] Testimony of R.J. Calloway before CPUC, filed July 5, 1983 in A.83-01-022, at 51, a document of public record judicially noticeable by this Court.

precisely what the decree intended.[18] AT&T's POR,

[18] AT&T's apparent answer to appellants' claim is a bald effort to rewrite the MFJ. First, AT&T contends that the definition of CPE intended by the decree is not that actually contained in the decree but that employed in *Second Computer Inquiry*, 84 F.C.C.2d at 61 n.10, 88 F.C.C.2d at 513 n.1, which excludes complex intrasystem wiring from the term "CPE." AT&T fails to cite any authority for this contention and is unable to explain why neither the language of *Second Computer Inquiry* nor a reference to that decision appears in the definition of CPE contained in the decree.

Moreover, the FCC in its current phase of the *Second Computer Inquiry* has taken the view that intrasystem wiring is an integral part of complex CPE and therefore should be transferred to AT&T and deregulated at the same time and in the same manner as the CPE which it joins. AT&T has told the FCC that it would be illegal to order this type of transfer because the MFJ herein has assigned complex intrasystem wiring to the BOCs. AT&T apparently desires to use the FCC proceeding to limit the definition of CPE in this divestiture case and then use this divestiture case to limit the FCC's ability to define the concept of CPE to include intrasystem wiring in the *Second Computer Inquiry*.

Second, AT&T argues that complex intrasystem wiring and related installation costs are not "equipment" within the meaning of the decree. This unsubstantiated assertion is refuted by the common dictionary definition of "equipment" (Reply Comments, CPUC, at 21) and by generally accepted accounting principles which include installation and connection costs as an integral part of the cost of a telecommunications system (*id.* at 21-22). Indeed, the notion that equipment costs include all expenditures incurred in acquiring the equipment and preparing it for use is forcefully confirmed by the decree's mandate that AT&T is to receive all "facilities . . . and books of account . . . *relating to . . . the provision of* customer premises equipment to the public."

Third, AT&T contends that the term "route" contained in the decree's definition of CPE refers solely to switching equipment and not to wire which carries a telecommunication toward its intended destination. Again, however, AT&T provides no authority for its assertion, nor does it offer any explanation as to why the term "switch," if truly intended, was not employed in the decree.

Finally, AT&T raises the "practical" claim that the varying elements of Account 232 cannot be separated out in a way which would meaningfully differentiate between the various assets it contains. This assertion is incorrect, as is demonstrated in Section IIA, *supra*. Even if the assertion were correct, which it is not, a credible argument could be made that all of Account 232 (or at least the subclass "Station Connections—Inside Wiring"), being an investment related to the provision of CPE, should be assigned to AT&T.

however, has retained what it deems the favorable CPE assets and has left to the BOCs what it deems the unfavorable assets, such as the complex intrasystem wiring investment reflected in Account 232. Appellants' sole remaining remedy for such manipulation of the decree is this appeal.

### III. Cost of Debt

Section VIII(H) of the MFJ provides in part:

> [T]he quality of debt [of the separated BOCs] shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time.

(App. at 184-185).

The POR, consistent with the foregoing directive, states that "[t]he debt remaining with the BOCs upon divestiture will be representative of the average terms and conditions of debt throughout the Bell System." (POR, §I(B)(4), at 193-194.) Nevertheless, the POR goes on to ignore the most significant "term" or "condition" of a debt instrument—the rate of interest that it bears—and proposes a distribution of long-term funded debt which would leave Pacific with a significantly higher average cost of debt than any of the other regional BOCs and the Bell System as a whole. (*Id.*, at 194-195.) AT&T's stated rationale for its proposal, that "[a]ny attempt to equalize the costs among regions and companies would introduce a number of subsidies between and among the divested BOCs" (*id.*, at 195), makes no sense. Section VIII(H) of the decree was intended to protect the BOCs from AT&T's leaving them with debt obtained at unfavorable terms and conditions while assigning to itself debt carrying more advantageous terms. (App. at 135-137.) AT&T's

assumption of such higher-cost debt as will leave Pacific with an average cost of debt reasonably comparable to that of the other six BOCs and the Bell System as a whole will in no way affect the other BOCs; it will merely affect AT&T. (Prelim. Comments, CPUC, at 24-25; Further Comments, CPUC, at 47-48; Reply Comments, CPUC, at 9-13.)

AT&T claims that different treatment is warranted for Pacific than for the other BOCs because Pacific holds a less favorable financial position than the other BOCs due to actions of local regulators, such as appellant CPUC. (AT&T Response, at 285-298.) This claim is wholly lacking in merit. First, it is factually misleading: Pacific's present disadvantaged financial position is plainly due most directly to AT&T's historic failure to invest any equity in Pacific during the years 1973 to 1981. (Prelim. Comments, CPUC, at 15-23.) Second, the decree itself already accords Pacific different treatment than the other BOCs, if any such different treatment is warranted, by authorizing AT&T to leave Pacific with a higher debt ratio (50%) than the other BOCs (45%). (MFJ, §VIII(H); App. at 184.) Accordingly, AT&T's justification for unilaterally rewriting the MFJ's "terms and conditions" provision in its POR has already been addressed by a separate provision of the MFJ. (*See* App. at 136-137 and 137 n.320.) Third, since the Bell System, prior to divestiture, is essentially a single entity, it is the system as a whole that must bear the cost of its pre-divestiture debt portfolio, the parts of which were obtained at different times and places and on different terms and conditions. Notably, in approving the POR's allocation of contingent antitrust liabilities, the District Court *accepted* this very reasoning. (App. at 214-219.)

In view of the foregoing and the virtual concession by the Department of Justice that the POR violates the decree (DOJ Response, at 117-122),[19] the District Court's footnote disposition of appellants' claim is difficult to comprehend (App. at 221-222 n.64).

The decree established a fair balance to which the POR was supposed to adhere; no legitimate basis for a variance was offered; and appellants presented the District Court with a simple and straightforward approach which would have effectuated the decree's requirements. (*See* Prelim. Comments, CPUC, at 28-30; Reply Comments, CPUC, at 11-13.)[20] Nevertheless, the District Court's ruling ratifies what is effectively a unilateral appropriation by AT&T of assets which the decree rightfully bestows upon Pacific.

Absent action by this Court, the ultimate losers will be the citizens and ratepayers of the Pacific region.

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[19] The Department of Justice twice asked the District Court to grant a formal exception to the decree as described in §VIII(H) thereof (DOJ Response, at 118, 122), but the District Court never did so (App. at 221-222 n.64).

[20] Appellants submit the following example of how the inequity may easily be corrected: Under Amendment No. 36 to the POR, AT&T has agreed to assume five long-term debt issues of Pacific's, bringing Pacific's average cost of debt to approximately 9.5 percent. One of those issues bears a maturity date of 2015, a face amount of $300 million and a coupon rate of 8.875 percent. However, if AT&T were instead to assume two separate outstanding $150 million issues—one bearing a maturity date of 2020 and a coupon rate of 15 percent and the other bearing a maturity date of 2021 and a coupon rate of 16.125 percent—Pacific's cost of debt would markedly improve.

While the implementation of this suggestion would still leave Pacific with an average cost of debt of 9.2 percent—substantially greater than the average cost of debt of any of the other BOCs or the Bell System as a whole—it would certainly bring the plan closer to compliance with the MFJ. It is estimated that this adjustment would reduce Pacific's annual long-term cost of debt by more than $20 million, without necessitating any subsidy from the other BOCs.

## IV. Plenary Review is Essential

The District Court's order of August 5, 1983, approving the details of the largest corporate reorganization in history, raises subtle, complex and difficult questions of compliance with the decree previously affirmed by this Court as well as broader questions concerning the adequacy of the District Court's protection of the public interest.

The only check on the District Court's ruling is the availability of careful review of the merits of appellants' claims by at least one appellate tribunal. While this Court's exercise of jurisdiction under 15 U.S.C. §29(b) would undoubtedly expedite the resolution of any uncertainties generated by the pendency of this appeal (*see generally* DOJ Motion for Certification, AT&T Response in Support), appellants neither sought nor participated in the District Court's certification decision because they considered the need for detailed review of their claims, whether by this Court or by the Court of Appeals, paramount. In a case as important as this one, considerations of expediency should not outweigh appellants' right to assert fully their public interest claims on appeal. Accordingly, should the Court for any reason determine not to accord appellant's claims plenary consideration, its fairest course would be to *deny* the direct appeal under 15 U.S.C. §29(b) and to remand the appeal to the United States Court of Appeals for the District of Columbia Circuit for decision only after full briefing and oral argument on the merits.

## Conclusion

For the foregoing reasons, the Court should note probable jurisdiction.

Dated: November 2, 1983

Respectfully submitted,

JANICE E. KERR*
J. CALVIN SIMPSON
GRETCHEN DUMAS
MARK FOGELMAN
5066 State Building
San Francisco, California 94102
(415) 557-0470
*Attorneys for Appellants*

* *Counsel of Record*

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Nos. _____

Office-Supreme Court, U.S.
FILED
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CLERK

IN THE

# Supreme Court of the United States

October Term, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE AND TELEGRAPH COMPANY, *et al.*,

*Appellees.*

---

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,

*Appellant,*

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE AND TELEGRAPH COMPANY, *et al.*,

*Appellees.*

---

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA.

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## APPENDIX TO JURISDICTIONAL STATEMENTS OF THE PEOPLE OF THE STATE OF CALIFORNIA, THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA AND THE NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE

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DAVID E. BLABEY
LAWRENCE G. MALONE
TIMOTHY P. SHEEHAN

Three Empire State Plaza
Albany, New York 12223
(518) 474-2510
*Attorneys for the New York State Department of Public Service*

JANICE E. KERR
J. CALVIN SIMPSON
GRETCHEN DUMAS
MARK FOGELMAN
5066 State Building
San Francisco, California 94102
(415) 557-0470
*Attorneys for the People of the State of California and the Public Utilities Commission of the State of California*

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# OPINION DENYING APPROVAL OF PROPOSED MODIFICATION OF FINAL JUDGMENT AND RECOMMENDING CHANGES

(Filed: August 11, 1982)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

| | |
|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INC.; AND BELL TELEPHONE LABORATORIES, INC.,<br>Defendants. | Civil Action No. 74-1698 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

## OPINION

These actions are before the Court[1] for a determination whether a consent decree proposed by the parties is in the "public interest"[2] and should therefore be entered as the Court's judgment. Over six hundred comments from interested persons, many of them objecting to various aspects of the proposal, have been received, and the Court has considered briefs submitted by the parties and others, and it has heard extensive oral argument. This opinion discusses the principal questions raised by these interested persons, and it embodies the Court's decision on the appropriateness of the proposed decree under the Tunney Act's public interest standard.

The opinion is divided into twelve parts. Part I relates the history of the litigation and the terms of the proposed decree. The next two sections contain analyses of two underlying legal issues — the standard of review to be applied by the Court under the Tunney Act (Part II) and the relationship between the decree and state regulation (Part III). The following section (Part IV) considers the question whether the divestiture of the local Operating Companies is in the public interest. Two sections discuss the removal of restric-

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[1] A number of prior opinions of this Court deal with earlier phases of these cases. The principal opinions in that category are reported at 461 F. Supp. 1314 (D.D.C. 1978) and 524 F. Supp. 1336 (D.D.C. 1981). Other opinions and memoranda may be found at 1982-1 Trade Cas. ¶ 64,623 (D.D.C. 1982); 1982-1 Trade Cas. ¶ 64,522 (D.D.C. 1982); 1982-1 Trade Cas. ¶ 64,521 (D.D.C. 1982); 1982-1 Trade Cas. ¶ 64,476 (D.D.C. 1982); 1982-1 Trade Cas. ¶ 64,465 (D.D.C. 1982); 524 F. Supp. 1381 (D.D.C. 1981); 524 F. Supp. 1331 (D.D.C. 1981); 1981-2 Trade Cas. ¶ 64,203 (D.D.C. 1981); 516 F. Supp. 1237 (D.D.C. 1981); 1981-1 Trade Cas. ¶ 63,987 (D.D.C. 1981); 1981-1 Trade Cas. ¶ 63,938 (D.D.C. 1981); 1980–81 Trade Cas. ¶ 63,711 (D.D.C. 1981); 1980–81 Trade Cas. ¶ 63,705 (D.D.C. 1981); 1980–81 Trade Cas. ¶ 63,696 (D.D.C. 1980); 88 F.R.D. 47 (D.D.C 1980); 498 F. Supp. 353 (D.D.C. 1980); 86 F.R.D. 603 (D.D.C. 1980); 1980-1 Trade Cas. ¶ 63,244 (D.D.C. 1980); 84 F.R.D. 350 (D.D.C. 1979); 83 F.R.D. 323 (D.D.C. 1979); and 86 F.R.D. 603 (D.D.C. 1979).

[2] Antitrust Procedures and Penalties Act, 15 U.S.C. §§ 16(b)–(h) (hereinafter referred to as the Tunney Act). See Part I(C) and II *infra*. The statute was sponsored by Senator Tunney of California.

tions from AT&T — Section V as a general matter, and Section VI in the context of the provision of information and of electronic publishing services. The next two sections directly relate to the Operating Companies: Section VII considers whether the proposed limitations on Operating Company activities are in the public interest and Section VIII whether the decree makes adequate provision for access by intercity carriers to Operating Company networks. Part IX discusses the issues arising from the division of assets between AT&T and the Operating Companies; Part X considers special issues and provisions; and Part XI deals with problems of implementation and enforcement. Part XII contains the Court's summary and conclusion.

## I
## PRELIMINARY CONSIDERATIONS

### A. History of the Litigation

On January 14, 1949, the government filed an action in the District Court for the District of New Jersey against the Western Electric Company, Inc.[3] and the American Telephone and Telegraph Company, Inc. (Civil Action No. 17-49).[4] The complaint alleged that the defendants had monopolized and conspired to restrain trade in the manufacture, distribution, sale, and installation of telephones, telephone apparatus, equipment, materials, and supplies, in violation of sections 1, 2, and 3 of the Sherman Act, 15 U.S.C. §§ 1, 2, and 3.[5] The relief sought included the divestiture by AT&T of its stock ownership in Western Electric; termination of exclusive

[3] Western Electric is the wholly owned subsidiary of AT&T that manufactures telecommunications equipment for AT&T's Long Lines Department and the Operating Companies. In addition, Western Electric provides telecommunications equipment and services to government agencies and, to a limited extent, the independent telephone companies.

[4] After the transfer of the action to this Court (see pp. 17–18 *infra*) it was docketed here as Civil Action No. 82-0192. The 1949 lawsuit will generally be referred to herein as the "*Western Electric* action."

[5] The action thus focused on the practices of defendants with respect to the telecommunications equipment industry.

relationships between AT&T and Western Electric; divestiture by Western Electric of its fifty percent interest in Bell Telephone Laboratories;[6] separation of telephone manufacturing from the provision of telephone service; and the compulsory licensing of patents owned by AT&T on a nondiscriminatory basis.

The court record reveals little activity in the case between the date of the filing of the complaint in 1949 and the entry of a consent decree in 1956. Except for the notation that an answer was filed in April, 1949, there are no record entries until the Fall of 1951 when the government filed and the court ordered compliance with several discovery requests. Following the discovery order, there is another two-year gap, and it is not until April 27, 1953, that another record entry is found. This entry indicates that defendants were given two additional months to complete their compliance with the government's 1951 discovery requests. The next reference is to the transcript of a hearing held on January 24, 1956, during which the consent decree was approved as being in the public interest. See pp. 7-8 *infra*.

The gaps in the court record are partly filled by a report of a committee of the United States House of Representatives[7] which conducted an intensive investigation of the circumstances surrounding the entry of the consent decree. Report of the Antitrust Subcommittee of the House Committee on the Judiciary on the Consent Decree Program of the Department of Justice, 86th Cong., 1st Sess., January 30, 1959 (Committee Print) [hereinafter Subcommittee Report]. That report reveals that the parties were quite active between the time of the filing of the government's discovery requests in 1951 and the signing of the consent decree in 1956.

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[6] Bell Telephone Laboratories, AT&T's telecommunications research and development facility, is a jointly owned subsidiary in which AT&T and Western Electric each own 50 percent of the stock.

[7] In a Tunney Act proceeding the Court is not limited by the rules of evidence but may take into account facts and other considerations from many different sources. See, *e.g.*, 15 U.S.C. § 16(f).

As early as February 28, 1952, the president of Bell Laboratories, Dr. M. J. Kelly, met with Secretary of Defense Robert A. Lovett and other members of the Department of Defense to enlist their help in persuading the Justice Department to suspend prosecution of the action[8] until the end of the Korean War,[9] a suspension the Attorney General refused to grant.[10]

AT&T continued its attempts to end the litigation as soon as the Eisenhower Administration took office. Its executives and lawyers met with officials of the Departments of Defense and Justice throughout the first six months of 1953. Subcommittee Report at 51-52. These efforts culminated in a meeting on June 27, 1953, during a judicial conference held at White Sulphur Springs, West Virginia, between T. B. Price, AT&T's general counsel, and Attorney General Herbert Brownell. According to a memorandum prepared by Price following this meeting, Attorney General Brownell said that he believed that "a way ought to be found to get rid of the case," and that AT&T "could readily find practices that [they] might agree to have enjoined with no real injury to [their] business." Memorandum of T. B. Price (March 3, 1954) *reprinted in* Subcommittee Report at 53-54.[11]

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[8] That same day, counsel for AT&T met with Attorney General J. Howard McGrath to make the same request, contending that the antitrust litigation was forcing key Bell Laboratories and Western Electric executives involved in important national defense projects to divert their attention from that work to preparations for trial. Subcommittee Report at 45-46.

[9] Secretary of Defense Lovett requested the postponement in a letter to the Attorney General dated March 20, 1952. As stated by the Committee,

> [i]ndefinite postponement was requested by the Defense Department despite the fact that neither Mr. Lovett . . . nor anyone else in the Department had made an independent investigation to determine whether trial of the suit would actually impede the mobilization effort or whether Bell System personnel working on defense matters would actually be needed for preparation of trial of the case.

Subcommittee Report at 47.

[10] The Defense Department continued to advocate this position for the remainder of 1952. Subcommittee Report at 51.

[11] In reviewing Price's memorandum and other information concerning

Shortly after this meeting, AT&T again urged the Defense Department "to intercede with the Justice Department to have the case settled on a basis that would not require divorcement of Western." Subcommittee Report at 55. To that end, Secretary of Defense Charles E. Wilson had a letter hand-carried to Attorney General Brownell urging him to end the litigation without divesting Western Electric. The rationale stated for this position was that the severance of Western Electric would "effectively disintegrate the coordinated organization which is fundamental to the successful carrying forward of these critical defense projects," and would be contrary to the vital interests of the Nation." Subcommittee Report at 56. The Wilson letter was actually prepared by AT&T.[12]

Periodic negotiations between AT&T and the government continued through 1954 and 1955, and by early December, 1955, the government and AT&T had reached an agreement.[13]

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the meeting, the Antitrust Subcommittee characterized the government's position as follows:

> There can be little doubt that by his statements to Mr. Price at the White Sulphur Springs meeting, Attorney General Brownell manifested a willingness to have the Justice Department consider a token settlement and forego a decree consistent with the public interest — an attitude denoting partiality toward the defendants incompatible with the duties of his public office.

Subcommittee Report at 55.

[12] During the summer of 1953, the Defense Department asked AT&T to prepare a memorandum explaining why that department should be interested in the termination of the antitrust litigation. AT&T obliged, and in early July, it provided the Defense Department with a memorandum which urged settlement of the suit without the divestiture of Western Electric. The memorandum was drafted in such a way as to make it appear that the Defense Department rather than AT&T has prepared it and, with two relatively minor exceptions, a letter identical to the memorandum was sent out the next week to the Attorney General over the signature of Secretary of Defense Wilson. Subcommittee Report at 55-56.

[13] The Subcommittee described in some detail how it uncovered evidence of the negotiating process between AT&T, the Department of Defense, and the Department of Justice. It appears that, as part of an attempt to investigate the Justice Department's policies and practices regarding antitrust consent decrees, the Subcommittee requested the Attorney

The consent decree which was the product of this process included neither the divestiture of Western Electric[14] nor any of the other structural relief originally requested by the government. Instead, an injunction was issued which precluded AT&T from engaging in any business other than the provision of common carrier communications services; precluded Western Electric from manufacturing equipment other than that used by the Bell System; and required the defendants to license their patents to all applicants upon the payment of appropriate royalties.

Despite the substantial differences between the structural relief requested in the government's 1949 complaint and the relief actually provided by the proposed decree, the District

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General make available the files relating to the negotiation and signing of the Western Electric consent decree. Subcommittee Report at X-XI. The Department refused to produce the files, and it also declined to supply answers to specific questions. According to the Subcommittee (Report at XIII), "[t]he extent to which the Department of Justice went to withhold information from the committee in this investigation is unparalleled in the committee's experience." In its view, the Department's reluctance to provide information "resulted from a desire to cover up those facts which the Department considered to be embarrassing." Subcommittee Report at XIII, 42.

Because of the Department's failure to cooperate, the subcommittee acquired the necessary information from "correspondence, memorandums [sic], and other files from AT&T, Western Electric Co., the Department of Defense, and the Federal Communications Commission." Subcommittee Report at XIV. Moreover, with regard to the information provided by the Defense Department, the subcommittee criticized that agency for providing the very same material to AT&T, even though it contained internal memoranda and correspondence between the Secretary of Defense and the Attorney General. Indeed, it appears that the Defense Department gave AT&T all of this material the day after AT&T made an oral request for the documents. Subcommittee Report at 43.

[14] The Justice Department contacted the Federal Communications Commission to determine the Commission's position on the issue of the divestiture of Western Electric, advising AT&T that it was doing so. AT&T immediately contacted each FCC Commissioner individually to convey the Bell System's position on the issue. Subcommittee Report at 71-73. Ultimately, the Commission informed the Justice Department that it did not regard the divestiture of Western Electric as essential.

Court for the District of New Jersey accepted the proposal on January 24, 1956, after a brief hearing, stating:[15]

> I feel that I can unhesitatingly accept the recommendation of the Attorney General, that this judgment is in the public interest, and that it is a satisfactory adjustment of this very, very vexatious problem; and I am therefore happy to go along with the recommendation made by the Attorney General and shall forthwith sign this judgment.

After the decree was approved, no major developments occurred in the case for the next several years. Until 1981, the entries in the court record[16] concern primarily the patent licensing provisions.[17]

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[15] *United States* v. *Western Electric Co.*, Civil Action No. 17-49, C.A. 82-0192, Transcript, January 24, 1956, at 5. The transcript of the hearing at which the decree was approved is six pages in length. The only substantive question the Court asked was whether the defendants would be required to provide patent licensees with "a general exposition of the know-how" in addition to providing them with manufacturing drawings, blueprints, and specifications. The government responded in the affirmative. This one assurance, however, appears to have been directly contrary to AT&T's interpretation of their obligation under the decree. During the House Subcommittee's hearings, Chairman Emanuel Celler criticized AT&T's counsel for failing to correct the court's misimpression, stating "[b]y your silence, it strikes me that there was something very much akin to deception on the court, because the court must have had an erroneous impression as to what the decree implied and he signed that decree." Hearings at 2258, *reprinted in* Subcommittee Report at 95-96.

[16] The only exception prior to 1980 is a dispute that occurred in the late 1960s when a private communications system carrier sought leave to intervene as a party plaintiff to challenge New Jersey Bell's offering of what the proposed intervenor characterized as a private communication system to hospitals in violation of the decree. The District Court denied the motion to intervene (*United States* v. *Western Electric*, C.A. No. 17-49, C.A. No. 82-0192, Order, February 26, 1968) and the Supreme Court affirmed (*Clark Walter & Sons, Inc.* v. *United States*, 392 U.S. 659 (1968).

[17] However, there was significant activity early in 1981. On May 2, 1980, the Federal Communications Commission had issued its so-called *Computer II* decision. *Second Computer Inquiry*, 77 F.C.C2d 384 (1980), *on reconsideration*, 84 F.C.C.2d 50 (1980), *on further reconsideration*, 88 F.C.C.2d 512 (1981), *appeal pending sub nom. Computer & Communications Industry Ass'n.* v. *FCC, et al.*, No. 80-1471 (and Consolidated Cases). In

This was the status of the *Western Electric* suit when the government filed a separate antitrust action on November 20, 1974, in this Court against AT&T, Western Electric, and Bell Telephone Laboratories, Inc. (Civil Action No. 74-1698).[18] The complaint in the new action alleged monopolization by the defendants with respect to a broad variety of telecommunications services and equipment in violation of section 2 of the Sherman Act. In this lawsuit, the government initially sought the divestiture from AT&T of the Bell Operating

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that decision, the FCC in essence modified the interstate telecommunications regulatory structure in three ways: first, it distinguished between basic transmission services traditionally provided by common carriers and enhanced network services such as those used for computer data processing; second, it found that enhanced services and customer premises equipment should not be regulated as common carrier offerings; and third, it concluded that AT&T should be allowed under the Communications Act to offer such services and such equipment but only through a fully separate subsidiary. The Computer and Communications Industry Association and others have appealed the *Computer II* decision to the Court of Appeals for this Circuit, and that appeal is still pending.

In the wake of the FCC's decision, AT&T and Western Electric on March 4, 1981, filed a "Motion for Construction" of the consent decree in the *Western Electric* case with the District Court in New Jersey requesting a ruling that the decree would not bar AT&T from furnishing the services authorized by *Computer II*. The motion was opposed by the government, but on September 4, 1981, the Court granted AT&T's request. *United States* v. *Western Electric Co.*, 1981-2 Trade Cases ¶ 64,275 (D.N.J. 1981). The government initially took an appeal to the Court of Appeals for the Third Circuit. On January 8, 1982, contemporaneously with the proposed settlement of these cases, the government and AT&T filed a joint motion to dismiss the appeal and to vacate as moot the District Court's order. The Third Circuit granted the motion on February 2, 1982, and on March 12, 1982, the District Court vacated its order. *United States* v. *Western Electric*, C.A. No. 17-49, C.A. No. 82-0192, Order, March 25, 1982.

[18] The government has indicated that it brought the 1974 suit because in its judgment the 1956 consent decree was not adequate to prevent activities that unreasonably restrained competition in telecommunications equipment markets, and did not protect against antitrust violations in the intercity telecommunications field. Competitive Impact Statement at 5 filed by the Department of Justice February 10, 1982. This Court has held that the 1956 decree did not bar the filing of the 1974 action under the doctrine of *res judicata*. *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1374. The 1974 lawsuit will generally be referred to herein as the "*AT&T* action."

Companies (hereinafter generally referred to as Operating Companies or BOCs)[19] as well as the divestiture and dissolution of Western Electric. While the action was pending, the government changed its relief requests several times asking, at various times or in various alternatives, for the divestiture from AT&T of Western Electric and portions of the Bell Laboratories.[20]

Pretrial discovery began shortly after the defendants filed their answer in February 1975, but during the next three-and-one-half years, that discovery was effectively halted for over thirty months.[21] On February 7, 1978, the Court referred the case to the Magistrate for preparation of a discovery schedule. Pursuant to that authority, the Magistrate issued two orders on April 27, 1978, but attempts at discovery led to various disagreements, and by the Summer of 1978, very little progress had been made.

On September 11, 1978, the Court issued an opinion which disposed of all then outstanding legal issues[22] and laid out the

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[19] The twenty-two Bell Operating Companies, most of which are wholly owned by AT&T, provide the means by which local telephone service is furnished. Bell customers presently also gain access to the network for both local and long distance telecommunications services through the Operating Companies. These Operating Companies are regulated by the various state public utility commissions. They may encompass several states, a single state, or only a single metropolitan area.

[20] The divestiture of all or at least some of the Operating Companies remained one of the government's principal alternative relief requests. See Part IV *infra*.

[21] Discovery was first stayed for almost twenty-two months while the Court resolved certain jurisdictional issues (Pretrial Order No. 1) and then again, this time by the Court of Appeals, while defendants appealed and then sought certiorari from an order this Court had issued on November 24, 1976.

[22] Three major legal issues were addressed, as follows: (1) whether the Court had jurisdiction over the action in light of the federal and state regulatory scheme; (2) whether all of the departments and agencies of the United States constituted the party plaintiff in this suit for purposes of discovery; and (3) whether the government could secure documents obtained in private antitrust suits against the defendants. Defendants unsuccessfully sought a writ of mandamus from the Court of Appeals and a writ of certiorari from the Supreme Court with respect to portions of the order.

future course of the pretrial proceedings. See *United States* v. *AT&T*, *supra*, 461 F. Supp. 1314. In brief, the proceedings were designed to coordinate discovery and the definition of issues and move both forward simultaneously and with expedition. To these ends, the parties were directed to file over the following eighteen months four[23] successive Statements of Contentions and Proof which precisely and in detail defined their legal and factual contentions.[24] Each Statement was to be more specific and more focused than the last, and discovery at each stage was to be limited to the issues raised in the most recent Statements.[25]

Upon the completion of this process, and pursuant to a further pretrial order, the parties began a structured stipulation process. This process was designed to produce, and it did produce, stipulations of all uncontested facts and contentions, a catalogue of all contentions that remained in dispute, and the proof (both testimonial and documentary) that would be used to support each contention. As a result of this process, the case was essentially divided into 82 segments or episodes,[26] many of which constituted major antitrust disputes in their own right. These episodes provided the structure for the presentation of evidence at trial.[27]

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[23] Ultimately only three Statements of Contentions and Proof were filed because the fourth Statement became unnecessary.

[24] Plaintiff's final Statement consisted of 1870 pages; defendants' third Statement of 2145 pages.

[25] To oversee discovery disputes, the Court relied upon the United States Magistrate and upon two Special Masters appointed by the Court. In Pretrial Order No. 16, the Court also ordered the Special Masters to supervise the judicial notice procedure established by the Court. The purpose of this procedure was to determine what documents would be admitted into evidence, notwithstanding their appearance as hearsay documents, for the truth of the matters stated therein. See *United States* v. *AT&T*, *supra*, 498 F. Supp. 353. For both discovery and judicial notice disputes, the parties could appeal the rulings of the Magistrate and of the Special Masters to the Court.

[26] The 82 episodes were recorded on over 4,200 computer printout pages. By the time of trial, some episodes and some contentions had been dismissed by the parties.

[27] For a more detailed explanation of this process, see *United States* v. *AT&T*, *supra*, 88 F.R.D. 47.

The trial itself began on January 15, 1981. At the request of the parties, the trial was recessed immediately after the opening statements[28] for a period of six weeks in order to afford an opportunity for a negotiated settlement.[29] When the settlement discussions proved fruitless, the trial resumed on March 4, 1981. The government presented close to one hundred witnesses, many thousands of documents, and additional thousands of stipulations. After the conclusion of the government's case, defendants moved to dismiss the action on a variety of grounds. That motion was denied on September 11, 1981. *United States* v. *AT&T*, *supra*, 524 F. Supp. 1336. Defendants commenced their case-in-chief on August 3, 1981, and during the next five months they presented approximately 250 witnesses[30] and tens of thousands of pages of documents.

Defendants were scheduled to complete the presentation of their evidence on about January 20, 1982, and it was expected that the government's rebuttal evidence would be presented between that date and February 10, 1982, when the trial would have ended. However, early in January, 1982, the Court was advised of the proposed decree described below.

B. The Proposed Decree

On January 8, 1982, the parties to these two actions filed with the District Court for the District of New Jersey a stipulation consenting to the entry by the Court of the

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[28] Under 15 U.S.C. § 16(a), in any civil or criminal antitrust suit brought by the United States, a final judgment or decree to the effect that a defendant has violated the antitrust laws "shall be prima facie evidence against such defendant under said laws as to all matters respecting which said judgment or decree would be an estoppel as between the parties thereto: *Provided*, That this section shall not apply to consent judgments or decrees entered before any testimony has been taken."

[29] Initially, only a two-week recess had been sought and granted, but this was subsequently extended to allow the incoming Reagan Administration and the new leadership of the Department of Justice to evaluate the pending settlement proposals. See this Court's Memorandum Orders of January 16 and January 30, 1981.

[30] The trial record in this case contains over 24,000 transcript pages.

"Modification of Final Judgment"[31] filed therewith.[32] On the same day, they attempted to file in this Court a dismissal of the *AT&T* action pursuant to Rule 41(a)(1)(ii), Federal Rules of Civil Procedure. This Court ordered that the dismissal be lodged, not filed,[33] and, in accordance with that order and the provisions of the Tunney Act, the dismissal has not yet been effected. See note 52 *infra*.

In their settlement proposal, the parties proposed that the Court enter the following judgment with respect to both lawsuits.[34]

Section I of the proposed decree would provide for significant structural changes in AT&T. In essence, it would remove from the Bell System the function of supplying local telephone service by requiring AT&T to divest itself of the portions of its twenty-two Operating Companies which perform that function.

The geographic area for which these Operating Companies would provide local telephone service is defined in the proposed decree by a new unit, the "exchange area." According to the Justice Department, an exchange area "will be large

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[31] The parties have designated their agreement as a "Modification of the Final Judgment." However, since the agreement encompasses far more than a modification of the 1956 judgment — and, indeed, as described at pp. 13–17 *infra*, deals primarily with the *AT&T* lawsuit — it would be misleading to refer to the agreement as a modification of the 1956 decree. The agreement will generally be referred to herein as the "proposed decree."

[32] The parties also filed a Memorandum suggesting procedures for evaluating the settlement proposal and a motion to transfer the *Western Electric* action to this Court. In addition, they filed a joint motion to dismiss the appeals pending in the Court of Appeals for the Third Circuit from the District Court's decision concerning the 1956 consent decree. See note 15 *supra*.

[33] Order filed January 8, 1982.

[34] The description of the agreement in this part of the opinion is general in nature, and it takes account neither of various qualifications and exceptions in the agreement itself nor of the possible impact of a plan of reorganization which AT&T will be required to submit later. These, more specific, issues are discussed in Parts IV through XI *infra*.

enough to comprehend continguous areas having common social and economic characteristics but not so large as to defeat the intent of the decree to separate the provision of intercity services from the provision of local exchange service."[35] Court approval would be required for the inclusion in an exchange area of more than one standard metropolitan area or the territory of more than one State.[36]

The Operating Companies would provide telephone service from one point in an exchange area to other points in the same exchange area — "exchange telecommunications"[37] — and they would originate and terminate calls from one exchange area to another exchange area — "exchange access."[38] The interexchange portion of calls from one exchange area to another exchange area[39] would, however, be carried by AT&T and the other interexchange carriers, such as MCI and Southern Pacific Co.[40]

The proposed decree sets forth general principles governing the configuration of the Operating Companies[41] which AT&T would be required to divest.[42] Under the proposal, AT&T

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[35] Competitive Impact Statement at 30. The exchange areas would generally be smalier than the area served by a so-called Class Four Office.

[36] AT&T would have the initial responsibility for drawing the boundaries of exchange areas, but its plan would have to be submitted to the Department of Justice for its approval.

[37] Also referred to herein as intraexchange service. This may roughly be equated with local telephone service.

[38] That is, they would provide local access to interexchange carriers.

[39] In general, this is the service commonly known as long distance service.

[40] The Operating Companies must also provide access services to link their subscribers with companies providing information services. This category of service, discussed in Part VI, *infra*, includes information retrieval, automatic telephone answering services, and electronic publishing.

[41] The number of new Operating Companies is not specified in the settlement proposal. AT&T has indicated that its reorganization plan will provide for the amalgamation of the twenty-two Operating Companies into seven regional Operating Comapnies.

[42] The proposal would permit AT&T to determine the method by which divestiture will take place.

would be required to endow the companies with sufficient personnel, facilities, systems, and rights to technical information to enable them to provide exchange telecommunications and exchange access services.[43] These personnel, systems, facilities and rights would be drawn from the Operating Companies and from AT&T and its other affiliates. AT&T would be permitted to choose to transfer some of these elements directly to the new Operating Companies and to place others in a central entity jointly owned by them.

AT&T would be required by the proposed decree to formulate a plan of reorganization which complied with these principles, and to submit the plan to the Department of Justice within six months after the Court approved the decree. The plan would not be effective without the Department's approval.

After divestiture, the new Operating Companies would be required to provide, through a centralized body, a single point of contact for national security and emergency preparedness. They would be permitted to use this or a similar central body to provide those services, such as administration and engineering, which "can most efficiently be provided on a centralized basis." In addition, until September 1987, AT&T, Western Electric, and Bell Laboratories would have to provide on a priority basis, all research, development, manufacturing, and other support services necessary to enable the Operating Companies to fulfill the requirements of the proposed decree.[44]

Section II of the proposed decree would complement these structural changes by various restrictions which are said to

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[43] If a facility had both intraexchange and interexchange functions, it could not be jointly owned by AT&T and the Operating Company, but it could be shared through a leasing or similar arrangement, provided the Operating Company retained control over the intraexchange portion of the facility.

[44] The proposal would further bar AT&T from reacquiring the stock or assets of the divested Operating Companies, and it would require the cancellation of the License Contracts between AT&T and the Bell Operating Companies and of the Standard Supply Contract between Western Electric and the Operating Companies.

be designed (1) to prevent the divested Operating Companies from discriminating against AT&T's competitors, and (2) to avoid a recurrence of the type of discrimination and cross-subsidization that were the basis of the *AT&T* lawsuit.

The first group of these provisions would require the divested Operating Companies to provide services to interexchange carriers[45] equal in type, quality, and price to the services provided to AT&T and its affiliates.[46] In addition, they would be prohibited from discriminating between AT&T and other companies in their procurement activities, the establishment of technical standards, the dissemination of technical information, their use of Operating Company facilities and charges for such use, and their network planning. The Justice Department has indicated that it intends these provisions to be "construed broadly to encompass all potential areas of favoritism, subtle as well as overt, that may arise in relationship between the divested BOCs and AT&T and its competitiors." Competitive Impact Statement at 26-27.

The second type of restriction imposed upon the Operating Companies is said to be intended to prevent them from engaging in any non-monopoly business so as to eliminate the possibility that they might use their control over exchange services to gain an improper advantage over competitors in such businesses. Thus, the Operating Companies would not be permitted (1) to manufacture or market telecommunications products and customer premises equipment; (2) to provide interexchange services, (3) to provide directory ad-

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[45] The information access functions performed by the Operating companies for providers of information services would also be subject to the equality requirement.

[46] Appendix B of the proposed decree describes in greater detail the requirement imposed by Section II on the Operating Companies to provide equal access to all interexchange carriers. According to the Competitive Impact Statement, these provisions are based on the principles (1) that the Operating Companies should have latitude to provide access in the manner they deem most efficient, (2) that they must meet performance and pricing criteria to ensure equal access, and (3) that a transition period is necessary to phase in these equal access requirements. See Part VII *infra*.

vertising such as the Yellow Pages; (4) to provide information services; and (5) to provide any other product or service is not a "natural monopoly service actually regulated by tariff." The Operating Companies would have the authority, however, to engage in what are called the "inherent" functions of procurement, engineering, marketing, and management.

Section III of the agreement provides that the decree would be binding on AT&T and the Operating Companies and their successors and that it would not constitute any evidence against, an admission by, or an estoppel against AT&T or the Operating Companies.[47]

The proposed decree contains a number of enforcement provisions. Section V would impose a requirement upon AT&T and the Operating Companies to inform their employees of their obligations under the decree. Section VI would grant to the Department of Justice the right of access to AT&T and the Operating Companies to inspect books, interview and depose employees, and demand reports.[48] Section VII provides that the Court would retain jurisdiction for the purpose of issuing orders to construe or carry out the settlement, to modify it, to enforce compliance, and to punish violations, upon application of the parties and, after the reorganization, upon the application of an Operating Company.

Finally, the proposed decree would vacate the final judgment entered on January 24, 1956 in the *Western Electric* case, eliminating the restrictions imposed upon AT&T by that decree.

On January 11, 1982, Judge Vincent Biunno of the District Court for the District of New Jersey, following a brief hearing, approved the proposed decree, interpreting it solely as a modification of the 1956 consent judgment, but he did not,

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[47] The limitation of the proposed decree's *res judicata* effect is apparently designed to prevent its use in private antitrust litigation as *prima facie* evidence of AT&T's liability pursuant to section 5(a) of the Clayton Act, 15 U.S.C. § 16(a). See note 25 *supra* and Part X *infra*.

[48] There are special exceptions for privileged materials, and information collected may not be disseminated except to the FCC and in connection with court proceedings to secure compliance.

initially, agree to the parties' request for a transfer of the *Western Electric* action to this Court.

The following day, this Court held a hearing and continued in effect its order that the stipulation of dismissal which the parties had attempted to file in the *AT&T* action here be simply lodged pending completion of the appropriate public interest proceedings. Judge Biunno thereafter granted the parties' motion for a transfer of the *Western Electric* action, that action was docketed here under Civil Action No. 82-0192 and, by order of this Court, it was consolidated with the *AT&T* action. At the same time, this Court vacated the order of January 11, 1982, which had approved the proposed decree, and it ordered that procedures equivalent to those required by the Tunney Act be applied to the consolidated actions.[49]

C. Procedures in Connection with the Settlement Proposal

The Tunney Act provides that a proposal for a consent judgment submitted by the United States in an action brought under the antitrust laws may not be entered by the Court without prior compliance with certain procedures. These procedures include a sixty-day comment period, publication of a competitive impact statement by the Department of Justice, a sixty-day period for the receipt of public comments, and a determination by the Court that "the entry of such judgment is in the public interest."[50] For the purpose of this public interest determination the Court may consider

> (1) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration or relief sought, anticipated effects of alternative remedies actually considered, and any other considerations bearing upon the adequacy of such judgment;

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[49] Order filed January 21, 1982. See Part I(C) *infra*.

[50] 15 U.S.C. § 16(e).

(2) the impact of entry of such judgment upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of public benefit, if any, to be derived from a determination of the issues at trial.

Procedurally the Court may

(1) take testimony of Government officials or experts or such other expert witnesses, upon motion of any party or participant or upon its own motion, as the court may deem appropriate;

(2) appoint a special master and such outside consultants or expert witnesses as the court may deem appropriate; and request and obtain the views, evaluations, or advice of any individual, group or agency of government with respect to any aspects of the proposed judgment or the effect of such judgment, in such manner as the court deems appropriate;

(3) authorize full or limited participation in proceedings before the court by interested persons or agencies, including appearance amicus curiae, intervention as a party pursuant to the Federal Rules of Civil Procedure, examination of witnesses or documentary materials, or participation in any other manner and extent which serves the public interest as the court may deem appropriate;

(4) review any comments including any objections filed with the United States under subsection (d) of this section concerning the proposed judgment and the responses of the United States to such comments and objection and

(5) take such other action in the public interest as the court may deem appropriate.

15 U.S.C. § 16(e), (f).

When they filed the present proposed decree, the government and AT&T took the position that the Tunney Act did not apply because (1) their submission in the District Court for the District of New Jersey was merely a "modification" of an existing consent judgment, as distinguished from the

entry of a judgment,[51] and (2) no consent judgment at all was filed in this Court, but only a dismissal of the pending action.[52]

In the opinion of this Court, that reasoning may most charitably be described as disingenuous. It that reasoning were deemed acceptable, the parties here — and in similar antitrust actions — could subvert the clearly expressed will

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[51] The theory apparently was that the Tunney Act does not apply to such modifications of existing decrees because most modifications are relatively minor and of interest only to the parties involved. There appears to be conflicting law on this subject. Compare *United States* v. *Motor Vehicle Manufacturers Ass'n.*, 1981-2 Trade Cas. ¶ 64,370 (C.D. Cal. 1981) with *United States* v. *Swift & Co.*, 1975-1 Trade Cas. ¶ 60,201 (N.D. Ill. 1975). Nevertheless, the government recognizes that when a major modification of an existing decree is proposed, the Tunney Act procedures "help facilitate thorough exposition and review." See Letter of Assistant Attorney General William F. Baxter to the Court (January 18, 1982). To this end, Tunney act or comparable procedures have been followed at least in cases where major modifications of decrees have been made. See note 67 *infra*.

[52] As the Court has previously commented (see Tr. 25040-45), there appear to be at least two problems with the parties' "dismissal" theory. First, for all intents and purposes, the settlement would dispose primarily not of the 1949 action (which matured into a consent decree in 1956 — 26 years ago) but of the lawsuit that at the time of the settlement was actively in trial and had been in trial for ten months. Indeed, as the recitation in Part I(B) above demonstrates, the proposed decree deals almost exclusively with *AT&T* — rather than *Western Electric* — issues. These basic facts cannot be obscured by the facile expedient of filing the proposal in New Jersey and denominating it a modification of the New Jersey decree. Second, while Fed. R. Civ. P. 41(a)(1) provides that the parties may file a dismissal without leave of court under certain circumstances, this may not be done where a statute provides otherwise. In the view of the Court, the Tunney Act is just such a statute.

Contrary to the parties' continued protestations that, notwithstanding these considerations, the *AT&T* litigation has been dismissed because they allegedly filed a dismissal notice, the lawsuit is pending and very much alive. As noted, this Court issued an order on January 8, 1982, that the dismissal notice was only to be lodged, not filed. Whatever may be the proper rule in other circumstances — a matter on which the Court expresses no opinion — at least when the dismissal of a major antitrust action has substantive aspects or is so closely tied to a "modification" of another decree as is the case here, Tunney Act procedures apply. The parties have not appealed the Court's decisions which refused the filing of the dismissal notice and required application of Tunney Act procedures.

of Congress by a mere act of labelling. The Tunney Act was designed to expose to public scrutiny and to a judicial public interest determination the settlements negotiated between the Department of Justice and the various antitrust defendants. The instant agreement, whatever the label the parties chose to affix, settled two such lawsuits. That settlement, moreover, not only disposed of what is the largest and most complex antitrust action brought since the enactment of the Tunney Act but the settlement itself raises what may well be an unprecedented number of public interest questions of concern to a very large number of interested persons and organizations. See note 60 *infra*. As the Court made clear from the very day the settlement was announced, it was not and is not prepared to allow this circumvention of the congressional purpose.[53]

In any event, the parties have now stated in various ways and before various forums (including before this Court) that, irrespective of their opinion of the technical applicability of the Tunney Act, they are willing[54] to have the Tunney Act procedures applied by this Court.[55] In view of those representations, it became unnecessary for the Court to pass specifically upon the technical applicability of the Act. Instead, the Court on January 21, 1982, entered an order which, pursuant to the parties' consent and the Court's general

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[53] Tr. 25039-46. See also Part II(A) *infra*.

[54] This willingness took especially concrete form after the Court expressed its views on the matter on January 12, 1982. See note 50 *supra;* letter from Assistant Attorney General Baxter to the Court (January 18, 1982); letter from Jim G. Kilpatrick, General Attorney for AT&T, to the Court (January 18, 1982).

[55] The parties have also stated that in their view the early approval by the New Jersey District Court of the settlement proposal does not preclude this Court from following the full Tunney Act procedures. See, *e.g.*, Response of the United States to Public Comments, May 20, 1982 [hereinafter Department of Justice Response to Comments]; Reply Comments of the American Telephone and Telegraph Co., May 21, 1982 [hereinafter AT&T Reply Comments]; letter of the parties to the Court dated January 18, 1982; statement of counsel for the parties, January 12, 1982 (Tr. 25,016-26).

equitable powers,[56] applied the substantive Tunney Act procedures to the instant settlement.

Following the entry of that order, and in compliance therewith,[57] the parties filed the appropriate pleadings and reports.[58] After the Court issued its January 21 order — and

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[56] See, *e.g.*, *United States* v. *Swift & Co.*, 1975-1 Trade Cas. ¶ 60,201 (N.D. Ill. 1975); *United States* v. *Ling-Temco-Vought, Inc.*, 315 F. Supp. 1301 (W.D. Pa. 1970); *United States* v. *F. & M. Schaefer Brewing Co.*, 1968 Trade Cas. ¶ 72,345 (E.D.N.Y. 1967); *United States* v. *Carter Products, Inc.*, 211 F. Supp. 144 (S.D.N.Y. 1962).

[57] However, on February 5, 1982, in its filing disclosing its lobbying activities in conformity with section 11 of the Court's order of January 21, 1982, AT&T stated that it made that filing "[i]n conformance with § 2(g) of the Antitrust Procedures and Penalties Act ('APPA'), 15 U.S.C. § 16(g)" rather than under the Court's order. In its subsequent public advertisements, AT&T has likewise taken the position that the settlement proposal is being reviewed by this Court "as provided in the antitrust statutes." See, *e.g.*, AT&T Advertisement "A Plea for Orderly Policy-making," *Washington Post*, March 28, 1982, at A28.

[58] On January 28, 1982, the government published the proposed decree in the Federal Register (47 Fed. Reg. 4166 (1982)); on February 5, 1982, AT&T filed with the Court its description of the written and oral communications made on its behalf with any officers or employees of the United States regarding the proposed decree; on February 10, 1982, the government filed with the Court its Competitive Impact Statement, and on February 17, 1982 published it in the Federal Register (47 Fed. Reg. 7170 (1982)); beginning on February 19, 1982, the government made copies of the proposed decree available at the twenty-six district courts specified in the Court's order of January 21, 1982; over a period of two weeks in February, 1982, the government published in newspapers of general circulation in these twenty-six districts, a summary of the proposed decree and the Competitive Impact Statement and directions for the submission of written public comments; from February 19 to April 20, 1982, there was a sixty-day public comment period; on April 21, April 23, April 27, and May 4, 1982, the government filed these written comments with the Court; as set forth in the Court's order of May 5, 1982 and in lieu of publishing all written comments, on May 10, 1982, the government issued a press release describing the procedures for obtaining copies of comments, and on May 17, 1982 published the press release in the Federal Register (47 Fed. Reg. 21214 (1982)); on May 17, 1982, the government published in the Federal Register the name and address of everyone who filed a written comment and the number of pages in each comment (47 Fed. Reg. 21214 (1982)); and on May 20, 1982, the government made available in each of the twenty-six districts referred to above a copy of every comment received.

even prior to that time[59] — a considerable number of individuals and entities sought to intervene in these proceedings for various purposes.[60] On February 5, 1982, the Court issued an order denying all such requests.[61] The Court also received

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[59] Those motions to intervene filed prior to the Court's issuance of the January 21 order were denied in that order.

[60] Among those who have sought to intervene, submitted procedural or substantive suggestions, or entered their appearances through counsel are the following: Alabama Public Service Commission; Alarm Industry Telecommunications Committee; State of California; Public Utilities Commission of California; Computers and Communications Industry Association; Continental Telephone Corporation; Independent Data Communications Manufacturers Association; Jack Faucett Associates, Inc.; the States of Maine, Alabama, Arizona, Colorado, Idaho, Illinois, Iowa, Louisiana, Maryland, Massachusetts, Minnesota, Montana, New Hampshire, New Mexico, North Dakota, Oregon, Rhode Island, Tennessee, Texas, Utah, Vermont, Washington, West Virginia, and Wyoming; MCI Communications Corp.; State of Michigan; Michigan Public Service Commission; State of Missouri; State of New York; New York State Consumer Protection Board; Public Service Commission of the State of New York; National Association of Regulatory Utility Commissioners; National Citizens Committee for Broadcasting; Public Citizen; Consumer Federation of America; Rep. Ron Mottl; Media Access Project; Consumer Utility Board of Wisconsin; State of New Mexico; North American Telephone Association; Southern Pacific Communications Corp.; Tandy Corp.; Tennessee Public Service Commission; U.S. Telephone Communications, Inc.; Public Service Commission of the District of Columbia; Public Advocate of New Jersey; Consumer Counsel of Ohio; National Association of State Consumer Advocates; General Communications, Inc.; Control Data Corp.; International Telephone and Telegraph Corp.; Federal Communications Commission; Illinois Commerce Commission; Citizens of the State of Florida; Office of Communications United Church of Christ; Public Service Commission of Wisconsin; General Telephone & Electronics Corp.

[61] The order explained that under the Tunney Act, permission to intervene is strictly within the Court's discretion; that it was premature to allow anyone to intervene because the public comment procedures provided ample protection for all legitimate interests at this stage of the proceedings; that at the end of the public comment period, the Court would establish a framework to ensure effective participation in further proceedings and would again consider what status should be given to participants; and that the denials to intervene were without prejudice to appropriate applications to intervene made at some later date.

Subsequent requests for intervention were disposed of on a similar basis. On March 25, 1982, for example, the Court denied the petition to intervene

a considerable number of comments from individual citizens. All such comments were filed in the Public Interest Docket,[62] and duplicates were turned over to the Department of Justice for its response in accordance with paragraph 8 of the January 21, 1982 order.[63]

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by the Public Service Commission for the District of Columbia and it reiterated (1) that there is no absolute right to intervene in these proceedings, and (2) that for the reasons stated in the February 5, 1982 order, no useful purpose would be served by allowing permissive intervention at this stage. Following the entry of that order, the Commission petitioned the United States Court of Appeals for a writ of mandamus directing this Court to permit it to intervene. In an order issued April 8, 1982, this Court denied a motion for a stay of all proceedings pending the appellate review, finding that none of the elements required for the granting of such relief had been satisfied. On June 1, 1982, the Court of Appeals denied the petition for a writ of mandamus, granted AT&T's motion to dismiss, and denied as moot the Commission's motion for a stay of proceedings, its motion for oral argument, and its motion to expedite appeal. In an accompanying Memorandum, the Court of Appeals stated "[w]e conclude that the District Court was correct in denying intervention of right at this stage of the proceedings." *United States* v. *AT&T*, C.A. No. 82-1321, Order and Memorandum (D.C. Cir. June 1, 1982).

Petitions to intervene filed by other participants were denied in orders issued April 14, May 5, and June 4, 1982. In addition, on August 2, 1982, the Court of Appeals granted the motion of the State of Michigan to dismiss voluntarily its appeal of this Court's denial of its motion to intervene. *United States* v. *AT&T*, No. 82-1389 (D.C. Cir. Aug. 2, 1982). However, in an order issued May 25, 1982, which established further procedures to focus and sharpen the various issues raised during the public comment period, the Court invited all interested persons to apply for intervenor or amicus curiae status to the extent that they believed and could demonstrate that such status was necessary and appropriate to protect their particular interests. For subsequent developments regarding intervention, see Part XI *infra*.

[62] In its February 5, 1982 order, the Court established a separate docket, Misc. No. 82-0025 (PI), for the filing of all documents relating to the public interest proceedings. The documents in this file have been treated as part of the record and have been utilized by the Court in considering the various issues raised in the public interest proceedings. For this docket, normal filing rules were waived to permit maximum participation by individual citizens as well as by persons and organizations represented by counsel.

[63] On July 27, 1982, the chairman of the Subcommittee on Telecommunications, Consumer Protection, and Finance of the House Committee on Energy and Commerce, and four of his colleagues, forwarded to the Court

During the months of April and May, 1982, the Department of Justice filed with the Court the comments it had received during the preceding sixty days, and on May 20, 1982, it filed its response to those comments.[64]

On May 25, 1982, the Court issued a Memorandum governing further proceedings. The Memorandum identified a number of key issues that were raised by the comments and the responses, and it invited the parties and the various interested persons to brief these issues in a form more suitable to judicial adjudication than the necessarily somewhat diffuse comments. A hearing was held on June 29 and 30, 1982, at which time the issues were further elucidated and refined.[65] The Court's substantive conclusions based upon the comments, responses, briefs, oral arguments, and the entire record herein, are discussed below.

## II
## POWER OF THE COURT IN THIS PUBLIC INTEREST PROCEEDING

Under the Tunney Act, the Court may approve the decree proposed by the parties only if it first determines that such approval is "in the public interest."[66] Before discussing the substantive provisions of the proposed decree, it is appropriate to set out the standards which will guide the Court's public interest review.[67]

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a letter with a number of recommendations and copies of the subcommittee's hearings on H.R. 5158, a bill to amend the Telecommunications Act of 1934. Copies of the letter were served on counsel for both parties; the Court ordered a copy placed in the court jacket; and it has considered these views pursuant to subsection (f)(2) of the Tunney Act.

[64] The next day, pursuant to leave of Court, AT&T filed its own reply to the comments.

[65] Twenty counsel from eighteen organizations presented oral argument during this two-day hearing.

[66] 15 U.S.C. § 16(e). While the Court has not held that the Tunney Act applies of its own force in this case, it is following the requirements of the statute in these proceedings. See pp. 19–22 *supra*.

[67] The standards are the same whether the judgment is regarded as "new" or as a modification of the 1956 decree in the *Western Electric* action. See *United States* v. *Motor Vehicle Manufacturers Ass'n*, 1981-2 Trade

A. Purpose of the Tunney Act

In enacting the Tunney Act, Congress sought to ensure that the Justice Department's use of consent decrees in antitrust cases would fully promote the goals of the antitrust laws and foster public confidence in their fair enforcement.[68] The legislators found that prior practice, which gave the Department almost total control of the consent decree process, with only minimal judicial oversight, failed to accomplish these ends.

The legislative history shows that Congress was particularly concerned that the "excessive secrecy" of the consent decree process deprived the public of the opportunity to scrutinize and comment upon proposed decrees, thereby undermining confidence in the legal system.[69] In addition, the legislators found that consent decrees often failed to provide appropriate relief, either because of miscalculations by the Justice Department[70] or because of the "great influence and

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Cas. ¶ 64,370 (C.D. Cal. 1981) (applying Tunney Act); *United States* v. *General Electric Co.*, 1977-2 Trade Cas. ¶ 61,659 (E.D. Pa. 1977) (applying public interest test); *United States* v. *Swift & Co.*, 1975-1 Trade Cas. ¶ 60,201 (N.D. Ill. 1975) (applying public interest test). Courts have applied a stricter standard of review only when modifications of existing decrees are contested by one of the parties. See *United States* v. *Swift & Co.*, 286 U.S. 106 (1932); Note, *Construction and Modification of Antitrust Decrees*, 77 Colum. L. Rev. 296, 304 (1977).

[68] The importance of consent decrees as an antitrust enforcement tool — as evidenced by the fact that they were entered in approximately 80 percent of the government's cases at the time the Tunney Act was passed — was the source of much of the legislators' concern. See H.R. Rep. No. 93-1463, 93d Cong., 2d Sess. 6 (1974); 119 Cong. Rec. 3455 (1973) (Remarks of Sen. Gurney).

[69] 119 Cong. Rec. 24598 (1973) (Remarks of Sen. Tunney). See also 120 Cong. Rec. 36343 (1974) (Remarks of Rep. Mezvinsky); 120 Cong. Rec. 36343-44 (1974) (Remarks of Rep. Jordan).

[70] Senator Tunney stated:

> Regardless of the ability and negotiating skill of the Government's attorneys, they are neither omniscient nor infallible. The increasing expertise of so-called public interest advocates and for that matter the more immediate concern of a defendant's competitors, employees, or antitrust victims may well serve to provide additional data, analysis, or alternatives which would improve the outcome.

economic power" wielded by antitrust violators.[71] The history, indeed, contains references to a number of antitrust settlements deemed "blatantly inequitable and improper" on these bases.[72]

To remedy these problems, Congress imposed two major changes in the consent decree process. First, it reduced secrecy by ordering disclosure by the Justice Department of the rationale and the terms of proposed consent decrees and by mandating an opportunity for public comment.[73] Second, it sought to eliminate " 'judicial rubber stamping' of proposals submitted to the courts by the Department," by requiring an explicit judicial determination in every case that the proposed

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119 Cong. Rec. 3452 (1973). Senator Tunney further suggested that a lack of resources further hampered the Justice Department's enforcement efforts (119 Cong. Rec. 24600 (1973)) and that the Department sometimes simply did not insist upon sufficient remedial action by the defendant. 119 Cong. Rec. 24598 (1973).

[71] S. Rep. No. 93-298, 93d Cong., 1st Sess. 5 (1973); H.R. Rep. No. 93-1463, *supra* at 6. See also 120 Cong. Rec. 36341 (1974) (Remarks of Rep. McClory).

[72] 119 Cong. Rec. 24598 (1973) (Remarks of Sen. Tunney). References were made, among others, to *Cascade Natural Gas Corp.* v. *El Paso Natural Gas Corp.*, 386 U.S. 129 (1967), where the Supreme Court found that the Department of Justice had consented to a decree which completely failed to alleviate the conditions found to violate the antitrust laws; to the 1956 decree in the *Western Electric* action (see Part I *supra*); and to the questionable circumstances surrounding the consent decrees entered in 1971 in cases involving the International Telephone and Telegraph Corp. (see *The ITT Dividend: Reform of Department of Justice Consent Decree Procedures*, 73 Colum. L. Rev. 594, 603–06 (1973)). 120 Cong. Rec. 36342-43 (1974) (Remarks of Rep. Holtzman); 120 Cong. Rec. 36345 (1974) (Remarks of Rep. Gunter); *Antitrust Procedures and Penalties Act: Hearings on S.782 and S.1088 Before the Subcomm. on Antitrust and Monopoly of the Senate Comm. on the Judiciary*, 93d Cong., 1st Sess. 76, 120, 135–36, 142–43, 147, 163–64, 181 (1973) [hereinafter cited as Senate Hearings]; *Consent Decree Bills: Hearings on H.R. 9203, H.R. 9947, and S. 782 Before the Subcomm. on Monopolies and Commerical Law of the House Comm. on the Judiciary*, 93d Cong., 1st Sess. 162–68 (1973).

[73] 15 U.S.C. §§ 16(b)–(d), (g). These procedures have been fully applied in this case. See pp. 21–24, *supra*.

decree was in the public interest.[74] It is clear that Congress wanted the courts to act as an independent check upon the terms of decrees negotiated by the Department of Justice,[75] and this Court will review the instant settlement in that spirit.[76]

B. Factors to be Considered

Although the statute is explicit as to the Court's obligation to make a public interest determination, it provides relatively little guidance as to the meaning of "public interest" in this context.[77] What is clear is that, whatever other factors a

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[74] H.R. Rep. No. 93-1463, *supra* at 8. See also 120 Cong. Rec. 36344 (1974) (Remarks of Rep. Jordan); 119 Cong. Rec. 3452 (1973) (Remarks of Sen. Tunney). Thus, Congress rejected case law to the effect that courts should not "assess the wisdom of the Government's judgment in negotiating and accepting [a] consent decree." *Sam Fox Publishing Co.* v. *United States*, 336 U.S. 683, 689 (1961). See also *Swift & Co.* v. *United States*, 276 U.S. 311, 331–32 (1928). The statute represents an endorsement of the line of cases in which courts examined proposed consent decrees to determine whether they were in the public interest. *E.g.*, *United States* v. *Ling-Temco-Vought, Inc.*, 315 F. Supp. 1301 (W.D. Pa. 1970); *United States* v. *Carter Products, Inc.*, 211 F. Supp. 144 (S.D.N.Y. 1962). See Senate Hearings, *supra* note 7, at 147-48 (Testimony of Hon. J. Skelly Wright).

[75] Accord, *United States* v. *National Broadcasting Co.*, 449 F. Supp. 1127, 1142 (C.D. Cal. 1978); *United States* v. *Morgan Drive Away, Inc.*, 1976-1 Trade Cas. ¶ 60,949 at 69,191 (D.D.C. 1976); *United States* v. *Gillette Co.*, 406 F. Supp. 713, 715 (D. Mass. 1975).

[76] The Court's powers are not restricted by the circumstance that bills are pending in Congress concerning several of the issues raised in this case. The Tunney Act requires the Court to evaluate the decree proffered to it by the parties, and it is clear that it may not avoid this mandate merely because Congress might at some future date enact legislation in the same field. Just as the Court refused to delay the trial of the *AT&T* action when it was apprised of the possibility of legislative action (see order filed July 29, 1981; Transcript of Proceedings, July 29, 1981, at 8–10, 13–14) so it could not now abdicate its responsibilities with respect to the profferred decree because of possible future legislative activity. Congress may, of course, enact legislation overturning a decree entered by this Court.

[77] The statute specifies several criteria which a court "may" consider in making its public interest determination (see 15 U.S.C. §§ 16(e)(1), (2))

court may take into account, it must begin by defining the public interest in accordance with the antitrust laws. S. Rep. No. 93-298, *supra*, at 3; H.R. Rep. No. 93-1463, *supra*, at 11-12. It is therefore to the basic purposes of the antitrust laws that we must first turn.

The Supreme Court has repeatedly held that, in enacting the Sherman Act, Congress sought to "preserv[e] free and unfettered competition as the rule of trade." *Northern Pacific Railway Co.* v. *United States*, 356 U.S. 1, 4 (1958). See also *National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 692 (1978); *United States* v. *Crescent Amusement Co.*, 323 U.S. 173, 187 (1944). Competition has not been endorsed by the Congress and the courts as a purely academic matter. The need to safeguard free competition is a direct result of the fundamental premise of our economic system that

> unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions.

*Northern Pacific Railway Co.* v. *United States*, *supra*, 356 U.S. at 4. See also *National Society of Professional Engineers* v. *United States*, *supra*, 435 U.S. at 695.[78]

This policy is embodied in two types of legal standards — those applied to the liability phase of antitrust cases and those which govern the relief phase. Since the Court's determination here is concerned solely with remedies, the decisions granting relief after a finding of liability form the most relevant

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but the legislative history indicates that the listing of these factors was not meant to limit the court's inquiry. S. Rep. No. 93-298, *supra*, at 6; 120 Cong. Rec. 36344 (1974) (Remarks of Rep. Jordan); 119 Cong. Rec. 24599 (1973) (Remarks of Sen. Tunney). These criteria therefore cannot be regarded as embodying *the* standard against which a proposed decree is to be measured. For further discussion of these factors, see note 93 *infra*.

[78] There is an obvious conceptual similarity between competition in commerce as the foundation of our economic system and competition in ideas as the basis of our political system.

yardstick for determining whether the proposed consent decree will further antitrust policies, and the Court will therefore use these decisions as its basic standard.

Antitrust remedies, it is usually said, must "effectively pry open to competition a market that has been closed by defendants' illegal restraints." *International Salt Co.* v. *United States*, 332 U.S. 392, 401 (1947). See also 2 P. Areeda & D. Turner, *Antitrust Laws* § 327 (1978). A decree must "break up or render impotent the monopoly power found to be in violation of the Act,"[79] that is, it must leave the defendant without the ability to resume the actions which constituted the antitrust violation in the first place. For these reasons, the decree should not be limited to past violations; it must also effectively foreclose the possibility that antitrust violations will occur or recur. As the Court noted in *International Salt Co.* v. *United States*, *supra*, 332 U.S. at 400,

> it is not necessary that all of the untraveled roads to [anticompetitive conduct] be left open and that only the worn one be closed. The usual ways to the prohibited goals may be blocked against the proven transgressor.

See also *National Society of Professional Engineers* v. *United States*, *supra*, 435 U.S. at 697-98; *United States* v. *United States Gypsum Co.*, 340 U.S. 76, 88 (1950); *Associated Press* v. *United States*, 326 U.S. 1, 22 (1945); *United States* v. *Crescent Amusement Co.*, *supra*, 323 U.S. at 188; *United States* v. *United Shoe Machinery Corp.*, 110 F. Supp. 295, 346-47 (D. Mass. 1953), *aff'd*, 347 U.S. 521 (1954).[80]

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[79] *United States* v. *Grinnell Corp.*, 384 U.S. 563, 577 (1966). See also *United States* v. *United Shoe Machinery Corp.*, 391 U.S. 244, 251 (1968); *Schine Chain Theatres, Inc.* v. *United States*, 334 U.S. 110, 128-29 (1948).

[80] On this basis, the Court may at the relief stage prohibit practices which have not been found unlawful if such a prohibition is necessary to avoid the recurrence of monopolization. *United States* v. *United Shoe Machinery Corp.*, *supra*; see also *Hartford-Empire Co.* v. *United States*, 323 U.S. 386, 409 (1945). In addition, restraints may be imposed upon the defendant which are designed to allow the development of nascent competition within the relevant market. *Ford Motor Co.* v. *United States*, 405 U.S. 562, 575, 578 (1972).

While the issue of competition and the effects on competition which are at the heart of the antitrust laws should thus be deemed matters of paramount concern, it is clear from the cases that other factors are not irrelevant.[81] As the Supreme Court has put it, antitrust violations should be remedied "with as little injury as possible to the interest of the general public" and to relevant private interests. *United States* v. *American Tobacco Co.*, 221 U.S. 106, 185 (1911). See also, *United States* v. *E.I. duPont de Nemours*, 366 U.S. 316, 327-28 (1961). When choosing between effective remedies, a court should impose the relief which impinges least upon other public policies. *United States* v. *American Tobacco Co., supra; United States* v. *E. I. duPont de Nemours, supra; United States* v. *Terminal Railroad Ass'n*, 224 U.S. 383, 410 (1912).[82] Thus, the Court would be justified in rejecting the proposed decree or requiring its modification[83] if it concluded that the decree unnecessarily conflicts with important public policies other than the policy embodied in the Sherman Act.

C. Degree of Deference to the Proposal Submitted by the Parties

Where, as here, a court is evaluating a settlement, it is not as free to exercise its discretion in fashioning a remedy as it would be upon a finding of liability. For when parties enter into a consent decree, they

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[81] The parties to this litigation as well as most interested third persons have expressly recognized that, in assessing whether the proposed decree is in the public interest, the Court may consider factors other than its effect on competition.

[82] However, where only one form of relief will effectively remedy the antitrust violation, it is that relief which must imposed, regardless of its impact on other interests. *National Society of Professional Engineers* v. *United States, supra*, 435 U.S. at 697-98; *United States* v. *E.I. duPont de Nemours, supra*, 366 U.S. at 327-28.

[83] The Court has the power to insist that the proposed decree take account of these other values. See *United States* v. *Ling-Temco-Vought, Inc.*, 315 F. Supp. 1301 (W.D. Pa. 1970), where the court refused to enter a proposed consent decree until the parties acted to safeguard the pension rights of the employees of the defendant.

> waive their right to litigate the issues involved in the case and thus save themselves the time, expense, and inevitable risk of litigation. Naturally, the agreement reached normally embodies a compromise; in exchange for the saving of cost and the elimination of risk, the parties each give up something they might have won had they proceeded with the litigation.

*United States* v. *Armour & Co.*, 402 U.S. 673, 681 (1971). If courts acting under the Tunney Act disapproved proposed consent decrees merely because they did not contain the exact relief which the court would have imposed after a finding of liability, defendants would have no incentive to consent to judgment and this element of compromise would be destroyed. The consent decree would thus as a practical matter be eliminated as an antitrust enforcement tool, despite Congress' directive that it be preserved. See S. Rep. No. 93-298, *supra*, at 6; H.R. Rep. No. 93-1463, *supra*, at 6.

It follows that a lower standard of review must be applied in assessing proposed consent decrees than would be appropriate in other circumstances. H.R. Rep. No. 93-1463, *supra*, at 12. For these reasons, it has been said by some courts that a proposed decree must be approved even if it falls short of the remedy the court would impose on its own, as long as it falls within the range of acceptability or is "within the reaches of public interest." *United States* v. *Gillette Co.*, 406 F. Supp. 713, 716 (D. Mass. 1975). See also *United States* v. *Bechtel Corp.*, 648 F.2d 660, 666 (9th Cir. 1981); *United States* v. *Carrols Development Corp.*, 454 F. Supp. 1215, 1222 (N.D.N.Y. 1978); *United States* v. *National Broadcasting Co.*, 449 F. Supp. 1127, 1143 (C.D. Cal. 1978). Although these decisions are not necessarily binding,[84] this Court will follow a similar approach.

It does not follow from these principles, however, that courts must unquestioningly accept a profferred decree as long as it somehow, and however inadequately, deals with the antitrust and other public policy problems implicated in the lawsuit. To do so would be to revert to the "rubber

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[84] There is no authoritative precedent from the Supreme Court or the Court of Appeals for this Circuit on this issue.

stamp" role which was at the crux of the congressional concerns when the Tunney Act became law. This consideration is especially potent in these cases, for several reasons.

First. This is not an ordinary antitrust case. The American Telephone and Telegraph Company, with its various components and affiliates, is the largest corporation in the world by any reckoning,[85] and the proposed decree, if approved, would have significant consequences for an unusually large number of ratepayers, shareholders, bondholders, creditors, employees, and competitors. Beyond that, it is clear that the divestiture of the Operating Companies, combined with the entry of AT&T into new competitive markets, will be an enormous undertaking, fraught not only with many problems and difficulties, but also with a potential for substantial private advantage at the expense of the public interest. In view of these considerations, and of the potential impact of the proposed decree on a vast and crucial sector of the economy and on such general public interests as the cost and availability of local telephone service, the technological development of a vital part of the national economy, national defense, and foreign trade, the Court would be derelict in its duty if it adopted a narrow approach to its public interest review responsibilities.[86]

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[85] The Bell System's total operating revenues in 1979 were over $45 billion, and in 1980, they exceeded $50 billion. These sums represent almost two percent of the gross national product of the United States in each of these years. The Bell System's net income for 1979 and 1980 was $5.6 billion and $6 billion, respectively. During 1979, the Bell System's net assets devoted to telephone service were valued at approximately $99.3 billion. At the end of 1979, the Bell System employed over one million people, and it was thus the largest employer in the United States with the exception of the federal government. Episode 5/57A, stipulation pars. 6, 8-9, 20. For a more impressionistic account of AT&T's size, see S. Kleinfeld, *The Biggest Company on Earth* (1982).

[86] There have been suggestions by some that the issues in these cases, involving as they do national telecommunications policy, should be left by the Court for Congress to decide. For the reasons stated in note 76 *supra* and otherwise, this is inappropriate. At the same time, a subject of this importance should not be decided solely by an agreement between the Department of Justice and a single company. The involvement of the Judiciary under the Tunney Act thus provides a useful safeguard.

Second. Some of those who during the legislative hearings took a narrow view of the judicial responsibilities under the Act suggested that the courts would generally not be able to render a sound judgments on settlements because they would not be aware of all the relevant facts.[87] But that factor is of relatively little relevance here, for this Court has already heard what probably amounts to well over ninety percent of the parties' evidence both quantitatively and qualitatively, as well as all of their legal arguments.[88] It is thus in a far better position than are the courts in the usual consent decree cases[89] to evaluate the specific details of the settlement.[90]

Third. These actions, and this settlement, have an unfortunate history. The 1956 *Western Electric* consent decree was evidently the product of the very kind of influence and pressure that Congress subsequently sought to prevent through the Tunney Act procedures. See pp. 3–7 *supra*. That identical settlement, and the identical parties, are now before the Court. Nor can those events simply be dismissed as ancient history, irrelevant to the events of 1981–82. One needs only to recall the peculiar circumstances under which the instant settlement proposal was sought to be filed in the courts[91] and the recurrence of an inappropriate collaboration in the course

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[87] See, *e.g.*, Senate Hearings, *supra* note 72, at 71.

[88] In addition, the Court has received comments and briefs concerning the proposed decree from several hundred interested persons, as well as voluminous submissions from the parties.

[89] In *United States* v. *Ling-Temco-Vought, Inc.*, *supra*, 315 F. Supp. at 1309, the absence of a record forced the court to rely upon the parties' assurances that the proposed decree was in the public interest.

[90] In fact, the parties sought review of the proposed decree in this Court precisely because of its "substantial expertise on the competitive situation in the telecommunications industry." Letter from Assistant Attorney General William F. Baxter, dated January 18, 1982.

[91] See pp. 19–21 *supra*. Because of the method the parties chose, that proposal might either have escaped Tunney Act review altogether or it might at best have been reviewed only to the extent agreeable to them. See, *e.g.*, the Memorandum in Connection with Stipulation and Modification of Final Judgment, filed by the parties in the District Court in New Jersey which refers to the procedures in restrictive terms, mentioning specifically only the publication and Federal Register requirements of the Tunney Act.

of the litigation between the Department of Defense and AT&T similar to that which occurred in 1952–54. See *United States* v. *AT&T*, 524 F. Supp. 1331 (D.D.C. 1981).[92] These circumstances do not foster a sense of confidence that the assessment of the settlement and its implications may be left entirely to AT&T and the Department of Justice.

None of this means, of course, that the Court would be justified in simply substituting its views for those of the parties. But it does mean that the decree will receive closer scrutiny than that which might be appropriate to a decree proposed in a more routine antitrust case.

The Court concludes that, taking into account the various legislative and decisional mandates discussed above, it will apply the following standard to its evaluation of the proposed decree. After giving due weight to the decisions of the parties as expressed in the proposed decree, the Court will attempt to harmonize competitive values with other legitimate public interest factors. If the decree meets the requirements for an antitrust remedy — that is, if it effectively opens the relevant markets to competition and prevents the recurrence of anti-competitive activity, all without imposing undue and unnecessary burdens upon other aspects of the public interest — it will be approved.[93] If the proposed decree does not meet

[92] See also note 145 *infra*.

[93] This standard encompasses the criteria specified in the Tunney Act except for "consideration of the public benefit, if any, to be derived from a determination of the issues at trial." 15 U.S.C. § 16(e)(2). This factor directs the Court to consider the effect of the proposed decree upon the ability of private antitrust plaintiffs to recover against the defendant for injuries alleged to have resulted from the activity challenged in the government. See 119 Cong. Rec. 3452 (1973) (Remarks of Sen. Tunney). However, the legislative history indicates that this is a secondary factor in the assessment of the decree and that the government's agreement to make information and evidence available to private plaintiffs will ordinarily be sufficient. S. Rep. No. 93-298, *supra* at 6-7; H.R. Rep. No. 93-1463, *supra* at 8.

The vigor with which several private plaintiffs have pursued actions against AT&T indicates that further prosecution of the government's case is not warranted on this basis. In addition, the Justice Department has indicated its willingness to provide trial record materials to private plaintiffs. Competitive Impact Statement at 49 n. 34.

this standard, the Court will follow the practice applied in other Tunney Act cases[94] and as a prerequisite to its approval, it will require modifications which would bring the decree within the public interest standard as herein defined.[95]

## III

## Conflict Between the Proposed Decree and State Regulation

A number of interested persons, principally States and state regulatory commissions,[96] contend that this Court lacks the power to enter the decree proposed by the parties without the approval of the regulatory commissions acting under state law. The decree would require AT&T to take various actions for which regulatory approval is required under state law,[97] and it would restrict the Operating Companies with respect to activities which they are authorized to engage in under state regulation.[98] Because of this conflict, say the States, the decree may not be entered until the requisite permission from the various state agencies has been secured. The Department of Justice and AT&T assert in response that state law[99] is preempted to the extent that it bars execution of the decree.[100]

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[94] See, *e.g.*, *United States* v. *Gillette Co.*, *supra*, 406 F. Supp. at 714-15.

[95] The Court finds no basis in law or policy for the suggestion made by the FCC and some others that it may have the power to modify the proposed decree over the objections of the parties and enter it on its own motion on that basis. If the parties decline to incorporate the Court's recommended modifications, the 1956 decree in the *Western Electric* action will remain in effect, the *AT&T* trial will resume, and the Court will then make its own decision as to liability and, if appropriate, as to remedy. In view of the substantial completeness of the record, the parties might elect not to adduce additional evidence, in which event the Court would make its decision based on the present record.

[96] All of these persons will be referred to hereinafter as the States.

[97] Such as transferring assets.

[98] For example, long distance telecommunications and provision of customer premises equipment.

[99] The District of Columbia Public Service Commission contends that the effect of the antitrust laws upon the District regulatory statutes cannot be

A. General

This is not the first case in which States have argued that a federal court decree based upon federal law may not validly require actions prohibited by state law. These claims are almost as old as the Republic. One needs to recall only the

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analyzed under the preemption doctine because both are congressional enactments. However, courts have characterized such local statutes as state laws for the purpose of reconciling them with national policies. See *D.C. Federation of Civil Associations, Inc.* v. *Volpe*, 434 F.2d 436 (D.C. Cir. 1970); *Columbia Plaza Limited Partnership* v. *Cowles*, 403 F. Supp. 1337, 1341 (D.D.C. 1975); *District of Columbia* v. *Greater Washington Central Labor Council*, 442 A.2d 110 (D.C. 1982). The preemption doctrine would thus be an appropriate gauge of Congress' intent concerning the relationship between the D.C. statute and the antitrust laws.

The recent decision in *Feldman* v. *Gardner*, 661 F.2d 1295 (D.C. Cir. 1981), *cert. granted on other grounds*, 50 U.S.L.W. 3998.09 (June 28, 1982), in which the court held that the District of Columbia Court of Appeals is immune from antitrust liability, does not require a different result. That case concerned antitrust *liability*, not the respect to be accorded District of Columbia statutes in implementing an antitrust *remedy*. In light of the *Feldman* Court's conclusion that the District "remains a federal enclave lacking the sovereignty inherent in statehood," it would be anomalous if statutes concerning purely local affairs could thwart vindication of a national policy when the statutes of the sovereign states cannot have such an effect. 661 F.2d at 1307.

[100] The Court must decide the preemption issue at this juncture even though no State has yet taken specific action which conflicts with the terms of the proposed decree. In the first place, many States have made it abundantly clearly that, unless the Court acts, they will proceed in a manner inconsistent with the decree. Further, the Court must delineate its powers now with respect to the conflicting state claims so as to avoid issuing an overbroad decree. Finally, the possibility that provisions of the decree could be vetoed by regulators on a state-by-state basis, with the resulting "balkanized scheme of telecommunications service" (Joint Comments of Alabama, et al., at 12) would obviously have a bearing on the basic question whether the proposed decree would and could effectively open the telecommunications industry to competition. If the States' claims are valid, the Court and the parties might have to search for different means to implement the mandate of the Sherman Act herein. It follows that a resolution of this legal issue is necessary if the Court is to render a proper determination under the Tunney Act. It may be noted, too, that the parties to the settlement as well as those who object thereto are in agreement that a decision by this Court at this time is both appropriate and necessary.

great school desegregation disputes of the last thirty years, in the course of which a number of States justified their failure to comply with federal court injunctions by asserting that compliance was impossible because of the conflicting requirements of state law. The Supreme Court repeatedly and consistently held that the Supremacy Clause of the Constitution[101] rendered invalid any state authority that conflicted with the federal court order. *North Carolina State Board of Education* v. *Swann*, 402 U.S. 43, 46 (1971); *Griffin* v. *County School Board*, 377 U.S. 218, 231-34 (1964); *Cooper* v. *Aaron*, 358 U.S. 1 (1958); see also *Morgan* v. *McDonough*, 540 F.2d 527 (1st Cir. 1976); *United States* v. *Indianola Municipal Separate School District*, 410 F.2d 626, 630-31 (5th Cir. 1969). More recently, in *Washington* v. *Washington State Commercial Passenger Fishing Vessel Ass'n*, 443 U.S. 658, 695 (1979), the Court once again rejected the argument that state law restrictions could provent a state regulatory agency from complying with a federal court's decree, reiterating that "[s]tate-law prohibition against compliance with the District Court's decree cannot survive the command of the Supremacy Clause of the United States Constitution."

While the basis for preemption is the Constitution, a preemptive effect in an individual case may be based on that document, on treaties, or on federal statutes such as the Sherman Act, which constitute valid exercises of federal power. See *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. 97 (1980). In other words, if this Court has the authority under the Sherman Act to issue the proposed decree, state regulatory statutes are unenforceable to the extent that they prevent compliance with its terms.[102]

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[101] Art. VI, cl. 2 states:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

[102] The fact that the decree would be issued pursuant to the parties' consent is irrelevant to its status, for a consent decree has the same effect as a decree issued after a finding of liability on the merits. *United States* v. *Swift & Co.*, 286 U.S. 106, 115 (1932). Accordingly, courts have found

The States cannot and most of them do not dispute that the conditions sought to be remedied by the decree fall within the broad sweep of the Sherman Act. Like the Commerce Clause of the Constitution,[103] the Sherman Act "extend[s] beyond activities actually *in* interstate commerce to reach other activities that, while wholly local in nature, nevertheless substantially *affect* interstate commerce." *McLain* v. *Real Estate Board of New Orleans, Inc.*, 444 U.S. 232, 241 (1980). See also *Hospital Building Co.* v. *Trustees of Rex Hospital*, 425 U.S. 738, 743 (1976). Similarly, the States do not dispute that the power of the Court under Section 4 of the Sherman Act, 15 U.S.C. § 4, to "prevent and restrain" violations of the statute is broad enough to encompass the decree proposed by the parties in this case. Their argument bypasses these general constitutional and antitrust principles to rely instead on certain specific aspects of the exercise of federal antitrust power, as follows.

1. *Tenth Amendment*

Several States assert — citing *National League of Cities* v. *Usery*, 426 U.S. 833 (1976) — that the proposed decree would unconstitutionally invade powers reserved to them under the Tenth Amendment. In that case, the Supreme Court held that Congress was foreclosed from extending minimum wage and maximum hour employment standards to persons employed by the States themselves, ruling (426 U.S. at 851-52) that activities in areas such as

> fire prevention, police protection, sanitation, public health, and parks and recreation . . . . are typical of those performed by state and local governments in discharging their dual functions of administering the public law and furnishing public services. Indeed, it is functions such

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that consent decrees displace state law to the same extent as do judgments on the merits. *Brown* v. *Neeb*, 644 F.2d 551, 563 (6th Cir. 1981); *United States* v. *American Society of Composers, Authors, and Publishers*, 442 F.2d 601 (2d Cir. 1971).

[103] Art. I, § 8, cl. 3. See *Heart of Atlanta Motel, Inc.* v. *Katzenbach*, 379 U.S. 241, 258 (1964); *Katzenbach* v. *McClung*, 379 U.S. 294 (1964); *Wickard* v. *Filburn*, 317 U.S. 111 (1942).

> as these which governments are created to provide, services such as these which the States have traditionally afforded their citizens. If Congress may withdraw from the States the authority to make those fundamental employment decisions upon which their systems for performance of these functions must rest, we think there would be little left of the States' 'separate and independent existence.' . . . [T]he dispositive factor is that Congress has attempted to exercise its Commerce Clause authority to prescribe minimum wages and maximum hours to be paid by the States in their capacities as sovereign governments. . . . We hold that insofar as the challenged amendments operate to directly displace the States' freedom to structure integral operations in areas of traditional governmental functions, they are not within the authority granted Congress by Art. I, § 8, cl. 3. (footnotes omitted).

The Court made it abundantly clear that its decision was not to be regarded as a wholesale retreat from the principle of federal supremacy in the event of federal-state conflict; rather, the decision was strictly limited to the proposition that the Tenth Amendment imposes limitations on the "exercise of congressional authority directed . . . to the States as States." *Id.* at 845.

The progeny of *National League of Cities* have continued to distinguish sharply between federal regulation of States and such regulation of "private persons and businesses 'necessarily subject to the dual sovereignty of the government and of the State in which they reside.' " *Hodel* v. *Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 286 (1981), *quoting National League of Cities* v. *Usery*, *supra*, 426 U.S. at 845. See also, *Federal Energy Regulatory Commission* v. *Mississippi*, 50 U.S.L.W. 4566 (June 1, 1982). As to the latter category of regulation, said the Court, there is "no Tenth Amendment impediment to congressional action." *Hodel* v. *Virginia Surface Mining & Reclamation Ass'n*, *supra*, 452 U.S. at 286.

The proposed decree imposes obligations only on private business. By its terms, it does not apply to the States at all; pursuant to the congressional power over interstate commerce

it simply regulates private activities which are without any doubt subject to that power. To be sure, some of these activities may also be subject to state regulation; but such confluence is not, and has never been held to be, regulation of "States as States."

The Supreme Court recently considered an analogous problem in *Federal Energy Regulatory Comm'n* v. *Mississippi*, *supra*. One of the statutory provisions at issue in that case permitted the Federal Energy Regulatory Commission to exempt certain private facilities from state laws. While the Court divided as to the application of the Tenth Amendment to other sections of the statute, it was unanimous in upholding this particular provision because, as the majority noted, "the Federal Government may displace state regulation even though this serves to 'curtail or prohibit the States' prerogatives to make legislative choices respecting subjects the States may consider important.' " 50 U.S.L.W. at 4570, quoting *Hodel* v. *Virginia Surface Mining & Reclamation Ass'n*, *supra*, 452 U.S. at 290. See also 50 U.S.L.W. at 4575 n. 1 (O'Connor, J., dissenting).

2. *Communications Act*

Some States argue next that in enacting the Communications Act, Congress intended to prevent federal preemption of the state regulation of telecommunications permitted by that statute. There is no evidence whatever to support this proposition. Absent specific indication of congressional intent, the Court declines to read the Communications Act so as to immunize these state laws from preemption by other federal statutes.

Furthermore, the States' authority under the Communications Act is limited to "local services . . . that in their nature and effect are separable from and do not substantially affect the conduct or development of interstate communications." *North Carolina Utility Commission* v. *FCC*, 537 F.2d 787, 793 (4th Cir. 1976). The decree, of course, concerns matters which are beyond this limited grant of jurisdiction.

Finally, even if the Communications Act did support certain kinds of state regulation, it would not help the States here.

This Court has heard a variation of the argument they make when it was raised, again and again, by AT&T and has rejected it every time. *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1345; *United States* v. *AT&T*, *supra*, 461 F. Supp. at 1320-30. As the Court previously stated, regulation under the Communications Act is neither sufficiently explicit nor sufficiently pervasive[104] to allow it to stand in the way of the enforcement of the antitrust laws.[105] All other courts which have had occasion in recent years to consider the subject of telecommunications antitrust immunity on account of regulation under the Communications Act have reached the same conclusion. *Phonetele, Inc.* v. *AT&T*, 664 F.2d 716 (9th Cir. 1981); *Sound, Inc.* v. *AT&T*, 631 F.2d 1324, 1327-31 (8th Cir. 1980); *Mid-Texas Communications Systems, Inc.* v. *AT&T*, 615 F.2d 1372, 1377-82 (5th Cir. 1980); *Essential Communications Systems, Inc.* v. *AT&T*, 610 F.2d 1114 (3rd Cir. 1979). See also, *National Gerimedical Hospital and Gerontology Center* v. *Blue Cross*, 452 U.S. 378 (1981). If the Communications Act itself and direct regulation by the FCC pursuant to that Act do not impair antitrust liability, *a fortiori* mere implied recognition in the Act of state regulation — assuming that there is such recognition — cannot stand in the way either of a finding of such liability or of the taking of necessary remedial action in implementation of the mandate of the Sherman Act.

B. Parker v. Brown

The States' primary contention is that the decree is barred by the state action exemption from the antitrust laws first announced in *Parker* v. *Brown*, 317 U.S. 341 (1943). In that case, the Supreme Court upheld a regulatory program which

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[104] See generally, *Gordon* v. *New York Stock Exchange*, 422 U.S. 659 (1975); *Otter Tail Power Co.* v. *United States*, 410 U.S. 366, 373-78 (1973).

[105] The Federal Communications Commission has consistently taken the same position. *In the Matter of Amendment of Subpart F of Part 1 of the Commission's Rules*, 42 F.C.C. 905, 906, 910-12 (1959); *In the Matter of the Applications of the Connecticut Water Co. & Woolridge Bros., Inc.*, 25 F.C.C. 1367, 1378 (1958). See also, Memorandum filed with this Court by the FCC as *amicus curiae* on December 30, 1975.

restricted competition among raisin growers by setting prices and limiting production. Finding no suggestion in the legislative history of the Sherman Act that such state action was to be restrained, the Court declined to find that the Sherman Act preempted the state law.

The *Parker* doctrine, which has been restated and applied a number of times since then,[106] "reflects Congress' intention to embody in the Sherman Act the federalism principle that the States possess a significant measure of sovereignty under our Constitution." *Community Communications Co.* v. *City of Boulder*, 50 U.S.L.W. 4144, 4147 (Jan. 13, 1982). See also Areeda, *"Antitrust Immunity for 'State Action' After Lafayette,"* 95 Harv. L. Rev. 435, 436 (1981). At the root of the rule is the principle that federalism permits the States to impose a regime of economic regulation which is different from and inconsistent with the free competition principle mandated by the antitrust laws.

There are several reasons why the States' reliance on the *Parker* doctrine is misplaced.

In the first place, since the doctrine in rooted in the desirability of state experimentation and regulation, it is not at all self-evident that it is applicable to the type of activity involved in these cases. The telecommunications network is, technologically and economically, a national network with interdependent components.[107] Congress has recognized this interstate characteristic, with its impacts on the national economy and national defense, by exercising its power under the Commerce Clause to reserve federal control over interstate communications. *North Carolina Utility Commission* v. *FCC*, *supra*. It may be doubted that the *Parker* doctrine

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[106] *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. 97 (1980); *New Motor Vehicle Board* v. *Fox*, 439 U.S. 96 (1978); *City of Lafayette* v. *Louisiana Power & Light Co.*, 435 U.S. 389 (1978); *Cantor* v. *Detroit Edison Co.*, 428 U.S. 579 (1976); see generally 1 P. Areeda & D. Turner, *Antitrust Law*, *supra* at §§ 212-220.

[107] Even after the division of the network into various separate entities as a result of the divestiture, it will still be a national network in its operational sense. See Part X(A) *infra*.

may reasonably be extended to this kind of an activity which is national par excellence.

In any event, the *Parker* v. *Brown* line of cases does not establish that all state regulation *per se* serves to immunize activities from the federal antitrust laws. Such an immunity exists only if (1) the restraint is clearly articulated and affirmatively expressed as state policy, and (2) the policy is actively supervised by the State. *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc., supra*, 445 U.S. at 105. Moreover, preemption is precluded only under special circumstances and to achieve a specific goal: to allow the states to implement alternatives to the Sherman Act system of free competition. It is against these standards that the States' contention here must be tested.

The conduct that is the subject of these antitrust actions is clearly not beyond the reach of the federal antitrust laws[108] — a conclusion with which the States are in agreement.[109] That is so because some of that conduct (*i.e.*, the allegedly anticompetitive activity of AT&T in the intercity services market) is not under state regulation at all; and because the remainder (*i.e.*, AT&T's activity in the local services and equipment markets) is regulated by the states only in the sense that the local Operating Companies are required to file tariffs with respect thereto — actions which the courts have consistently held to be insufficient to qualify under the *Parker-Midcal* "active supervision" standard.[110] To put it another

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[108] See *Phonetele, Inc.* v. *AT&T, supra; Sound, Inc.* v. *AT&T, supra*, 631 F.2d at 1327-31, 1334-35; *Essential Communications Systems, Inc.* v. *AT&T, supra*, 610 F.2d at 1125; *Northeastern Telephone Co.* v. *AT&T*, 477 F. Supp. 251 (D. Conn. 1978), *rev'd on other grounds*, 651 F.2d 76 (2d Cir. 1981); *United States* v. *AT&T, supra*, 461 F. Supp. at 1320-30.

[109] Brief on Topic Five of the Public Service Commission of Wisconsin, et al. at 8; Brief on Topic Five of State of California, et al., at 3.

[110] To be sure, the States are closely regulating such activities as the transfer of assets by entities within their jurisdictions and the types of business operations in which the Operating Companies may engage. But these subjects of state regulation are not the target of antitrust actions before the Court; the conduct that is being challenged is that of AT&T in the intercity services and equipment markets and, as indicated *supra*, that conduct is not being regulated by the States at all.

way, it is clear that state regulation would not be a defense during the liability phase of this or any other antitrust action based on similar conduct.

Since the conduct which is the subject of these lawsuits is thus well within the jurisdiction of the federal antitrust laws — as distinguished from the regulatory jurisdiction of the States — it would make no sense to hold that, in providing a remedy for the anticompetitive conduct,[111] the Court must refrain from interfering with state regulation.[112] Such a holding would in effect place this conduct in a non-man's land — not regulated by the states sufficiently to meet the *Parker-Midcal* test, yet immunized from effective federal antitrust jurisdiction because the antitrust remedy is barred by state regulations unrelated to this conduct.[113]

The practical consequences of such a rule to antitrust enforcement could be devastating.

No effective, unconditional antitrust judgment could be entered and enforced with respect to any subject matter area in which the states had established a system of regulation. The federal antitrust court would have to await the outcome, the benevolent agreement, of the local regulatory authorities before it could implement its decree. Should one or more States or their regulatory bodies object, the decree could not be enforced, irrespective of the necessity for such enforcement in the vindication of federal antitrust policy.[114] It is inconceivable that Congress could have intended to defer to state

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[111] The same rationale applies to its equivalent, a consent decree. Although the States' argument is directly addressed to the decree proposed by the parties, it is clear that the principle they espouse, if correct, would apply to judgments on the merits as well.

[112] It may be for this reason that no court has ever applied the *Parker* doctrine to thwart an antitrust remedy when the conduct in question was not shielded from liability.

[113] For example, in these cases, anticompetitive activity in the intercity carrier market would be protected because the remedy — divestiture — could be precluded by state regulations concerning the transfer of assets.

[114] An antitrust defendant would need to find just one sympathetic local regulatory body to achieve immunity from structural relief at the behest of a federal antitrust court.

laws in such a way as to preclude a court from effectively remedying an antitrust violation. Without effective relief, "the Government has won a lawsuit and lost a cause." *International Salt Co.* v. *United States*, *supra*, 332 U.S. at 401.[115]

Deference to state law in this type of situation would leave the Sherman Act powerless to eliminate anticompetitive activity,[116] even though the activity was not subject to state regulation sufficient to preclude application of the antitrust laws. This result is directly contrary to the thesis of the state action doctrine: that "[t]he national policy in favor of competition" is supplanted only when state regulation will take its place.[117] *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, *supra*, 445 U.S. at 106.

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[115] There is an obvious difference between direct state regulation and inchoate, general federal antitrust policy, on the one hand, and a conflict between such regulation and an explicit, valid federal court order, on the other. *Parker* deals only with the substantive scope of the antitrust laws, that is, with the situation which arises when a State has determined that, with respect to certain activities within its jurisdiction, the competition mandated by the Sherman Act is inappropriate for valid state public policy reasons. But there is nothing in the doctrine that would prevent the antitrust laws from prevailing when there is a conflict between a necessary antitrust remedy in a case in which the federal antitrust court has jurisdiction and in which the antitrust laws have been validly applied as a substantive matter and state regulatory schemes which would prevent such a remedy from being implemented. To hold otherwise, would be to stand proper deference to the policy of another political entity under the American constitutional system on its head.

[116] For example, the principal alternative to divestiture, a detailed injunction governing defendants' operations, would certainly conflict with state laws even more directly and on a continuing basis. While the remedy of damages would presumably still be available, it would not necessarily force defendants to cease any anticompetitive conduct. Moreover, there is no indication in the statute or in any court decision that the damages remedy is broader than the power to grant injunctive relief. The States' other alternative — an immediate spin-off of the Bell Operating Companies — would not open the telecommunications market to competition and would have severe adverse effects upon the national telephone system. See Part. XI(D) *supra*.

[117] Nothing in the proposed decree would require a State to replace its regulatory system with a system of competition: they may continue to

In these particular cases, the rule proposed by the States would reduce the Court's judgment to little more than an advisory opinion: AT&T would have to obtain the approval of the public utilities commission of every State before that judgment would actually be implemented. As the States themselves have said, if their claim were accepted, they would have the "unassailable authority to veto" the divestiture and to cause a "balkanized scheme of telecommunications service" should they so choose.[118]

The Court concludes that the state action doctine does not restrict the judicial power to impose an appropriate remedy under the Sherman act.

C. Avoidance of Unnecessary Conflict with State Law

The absence of absolute limitations upon a court's remedial powers under the Sherman Act does not mean that the court is free to ignore the States' legitimate interests.

It is well established that interference with state interests is not a favored approach; it is a measure to be employed only when necessary to vindicate federal law. Thus, a judicial remedy may infringe upon state law only to the extent necessary effectively to protect the federal interest. See *Milliken* v. *Bradley*, 433 U.S. 267, 280-81 (1977); *Morgan* v. *McDonough*, *supra*, 540 F.2d at 534.[119] Moreover, in exercising their discretion in fashioning antitrust remedies,[120] courts are obligated to minimize the impact of their decrees upon

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require a regulated monopoly in, say, local telephone service or intrastate toll service.

[118] See Joint Comments of Alabama and twenty-three other States at 12.

[119] It is presumably in reliance on these principles that the Department of Justice has conceded that "the Court should assure itself that the provisions of the proposed [decree] will not unnecessarily conflict with important state interests." Brief at 70. Another manifestation of the respect accorded to state interests is the courts' reluctance to impute to Congress an intent to bar the States from an entire field of regulation. See, *e.g.*, *Exxon Corp.* v. *Governor of Maryland*, 437 U.S. 117, 128 (1978); *Florida Lime & Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 142 (1963).

[120] See, *e.g.*, *Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at 573; *United States* v. *E. I. duPont de Nemours & Co.*, *supra*, 366 U.S. at 322.

other public policies (see Part II *supra*), including, of course, the policy against unnecessary interference with state interests.

Were the Court to fashion its own remedy following a finding of liability, it would accordingly be obligated to minimize interference with state law to the extent that may be done without vitiating or weakening the remedial measures required as a result of the findings made in the litigation. It is difficult to believe that when the parties arrive at a consent decree they have greater powers to override these principles than would the Court in drafting its own decree. In any event, whatever the parties may do, the Court would certainly be justified in taking the policy against unnecessary interference with state law and state policy into account when it passes upon the proposed judgment in a public interest proceeding.

It follows from what has been said that those provisions in the proposed decree which are necessary to vindicate the federal interest in the enforcement of the antitrust laws will be approved notwithstanding the fact that they may conflict with the state laws or interests. However, in its overall consideration of the public interest, the Court will also take into account that a particular provision may be merely peripheral to the federal interest but have a substantial adverse impact on state laws.[121]

## IV
## The Divestiture

A key feature of the proposed decree is the divestiture of the Operating Companies from the remainder of AT&T. In order to determine whether that divestiture is in the public interest, the Court must decide first whether it is a remedy that is likely to eliminate anticompetitive conditions within the telecommunications industry. In addition, the Court must assess the efficacy of alternative remedies, and it must also weigh the effect of the divestiture on the public interest

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[121] See Part VII *infra*.

generally, particularly on the level of charges for local telephone service.

A. Conditions Necessitating Antitrust Relief

1. *Evidence of Anticompetitive Actions by AT&T*

In its complaint and in documents filed thereafter (*i.e.*, the several Statements of Contentions and Proof), the government asserted that AT&T monopolized the intercity telecommunications market and the telecommunications product market in a variety of ways in violation of the Sherman Act.

The evidence that was produced during the *AT&T* trial indicates that, at least with respect to several of the government's claims, this charge may be well taken. It would be inappropriate for the Court at this juncture to draw definitive conclusions with regard either to the sufficiency of the evidence to sustain a finding of liability or to the validity of AT&T's various legal and factual defenses. The Court is not called upon, in this public interest proceeding, to render a final judgment on this case; indeed, not all the evidence that may bear on the issues has yet been adduced.[122] It is not improper, however, for the Court to consider whether the state of proof at trial was such as to sustain this divestiture as being in the public interest. See 15 U.S.C. §§ 16(b)(2), (e).

In its intercity case, the government alleged that AT&T used its control over its local monopoly to preclude competition in the intercity market. The government proved *inter alia* that after 1968 AT&T included a "customer premises" provision in its interconnection tariff which deterred potential competitors from entering the market;[123] that it refused to

[122] See p. 12 *supra*.

[123] Under this provision, a competitor could interconnect with the AT&T network only if the interconnection occurred in switching equipment located on the customer's premises where the telecommunication originated or terminated. The effect of this restriction was to prevent competitors from entering the intercity market gradually, and thus effectively from entering the market at all. For example, because of this restriction, a customer whose sole office was in St. Louis could not choose to use the services of an AT&T competitor for part of a route (*e.g.*, from St. Louis to Chicago),

provide FX and CCSA services to specialized common carriers and domestic satellite carriers until 1974 when the FCC specifically ordered it to do so;[124] and that it attempted to prevent competitors from offering metered long distance service that would compete with AT&T's own regular long distance service.[125]

AT&T's basic rationale for these policies was that it was attempting to prevent competitors from "creamskimming."[126] As viewed by AT&T, it would have been able successfully to combat creamskimming if it had priced each of its routes on the basis of the costs for operating that route. However, it concluded that the FCC had rejected this approach when it endorsed national rate averaging in the interest of promoting the goal of universal service. Accordingly, AT&T argued that, since rate averaging is inconsistent with competition, and since the basic rate averaging policy had been required

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and then AT&T's services for the remainder of the route (*e.g.*, from Chicago to Bethesda, Md.) because the St. Louis customer did not have the "premises" in Chicago that AT&T required for interconnection. Thus, to receive service for Bethesda as well as for Chicago, the customer was required to purchase both services from AT&T. See *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1354.

[124] FX (foreign exchange) service permits a customer to make or receive local calls through a distant switching center by effectively providing a long extension cord in the form of a dedicated line between the customer's location and a telephone company switching system in the distant location (the foreign exchange). See *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1355 n. 77. CCSA (common control switching arrangement) is essentially a miniature AT&T long distance network, except for the fact that it is used by only one customer, albeit a customer, such as the federal government, with large telecommunications needs.

[125] The government also alleged *inter alia* that AT&T discriminated against competitors in providing access to local exchange facilities; that it conducted interconnection negotiations with competitors in bad faith; and that it engaged in predatory behavior to eliminate at least one company as a provider of digital data transmission services. *United States* v. *American Telephone and Telegraph Co.*, *supra*, 524 F. Supp. at 1355-56.

[126] Creamskimming is a term the Bell System used during the *AT&T* trial and elsewhere to describe the practice of its competitors to concentrate their intercity services on routes where the volume of business is high and the costs of service are low.

by the FCC as being in the public interest, it was acting reasonably under the Communications Act in preventing competition as best and as long as it could.[127]

What this line of reasoning fails to consider is that, at least by the mid-1970s, the FCC had clearly begun to promote competition in telecommunications. The government contended during the trial — correctly, in the Court's view — that AT&T had an obligation to follow the more recent FCC policy rather than its previous policies which may have suited it better,[128] particularly since there was never a direct FCC rule against de-averaging. Moreover, even if, because of the lack of definite guidance from the FCC, AT&T's actions were to be regarded as reasonable under the Communications Act standards, it does not at all follow that these same actions were immunized under the standards of the Sherman Act.[129]

What is significant about these events is that AT&T was able to adopt the policies described above in large part because of its control over the local exchange facilities. For example, it was because of its ownership and control of the local Operating Companies — whose facilities were and are needed for interconnection purposes by AT&T's competitors — that AT&T was able to prevent these competitors from offering

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[127] See, *e.g.*, testimony of John D. deButts (August 27, 1981); Mark Garlinghouse (December 11, 1981); and William Ellinghaus (August 12, 1981).

[128] Obviously, AT&T preferred to operate as a monopoly provider of intercity services rather than to be forced to compete with other common carriers. (This is particularly true because once the FCC adopted a policy of competition, AT&T would be required to allow competitors to interconnect with the AT&T network). Thus, AT&T's self interest dovetailed neatly with its public interest argument.

[129] Under the antitrust laws, the burden would be on AT&T to show that what would otherwise be clearly unreasonable restraints on competition were cleansed by the regulatory directives. See, *e.g.*, *National Gerimedical Hospital and Gerontology Center* v. *Blue Cross*, 452 U.S. 378 (1981); *Sound, Inc.* v. *AT&T*, 631 F.2d 1324 (8th Cir. 1980); *Mid-Texas Communications Systems, Inc.* v. *AT&T*, 615 F.2d 1372 (5th Cir. 1980); *Essential Communications Systems, Inc.* v. *AT&T*, 610 F.2d 1114 (3rd Cir. 1979); *United States* v. *AT&T*, 524 F. Supp. at 1345, n. 14; *United States* v. *AT&T*, 461 F. Supp. at 1320-30.

FX and CCSA services. Similarly, AT&T was able to deter competition by manipulating prices for access to the Operating Company networks.[130]

AT&T's control over the local Operating Companies was central also to the anticompetitive behavior alleged with respect to the second facet of the government's case, that involving customer-provided terminal equipment.

The government proved that AT&T prohibited the attachment of competitors' equipment to the network except through a protective connecting arrangement (PCA). There was evidence that some experts (including a panel of the National Academy of Sciences)[131] believed that such a PCA was necessary[132] if the nationwide telephone network was to be protected from a variety of harms.[133] On the other hand, the government's evidence indicated that AT&T required PCAs for equipment that in all probability could not harm the network; that there were delays in providing PCAs; that the PCAs were over-designed and over-engineered, and, thus, over-priced; that PCAs were required for competitive equip-

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[130] See, *e.g.*, *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1364–65 n. 118; testimony of William Ellinghaus and Mark Garlinghouse on cross examination, note 127 *supra*. AT&T's cost data were often confusing, incomplete, and inaccurate, and although some of its distinguished economists provided helpful and sophisticated economic analysis (*e.g.*, William J. Baumol, December 7, 1981), others (*e.g.*, Jules Joskow, October 23, 1981) did little to explain away the shortcomings of these data. At least on the basis of the evidence heard before the trial was recessed, the Court would be unable to conclude that AT&T's past pricing strategy did not pose anticompetitive problems.

[131] See *Technical Analysis of the Common Carrier/User Interconnections Area* by the Panel on Common Carrier/User Interconnections, National Academy of Sciences (1970), PX781 (admitted in evidence on behalf of defendants at Tr. 13500, August 24, 1981).

[132] See, *e.g.*, testimony of Charles Elmendorf (November 17, 1981); Robert B. Brunson (August 25, 1981).

[133] Throughout the trial, AT&T referred to four harms to the network: hazardous voltages, longitudinal imbalance, excess signal power, and improper network control signaling. These harms, it was alleged, could cause a variety of problems, ranging from severe physical injury to humans to a small amount of noise on a telephone line.

ment while identical equipment sold by AT&T did not require their use; and that PCAs could not guard against all four potential harms to the network.[134]

Additionally, the alternative option of certification[135] was available but never seriously pursued by Bell.[136] Moreover, when ultimately certification was directly mandated by the FCC as a substitute for the protective connecting arrangement, the telephone network — AT&T's predictions to the contrary notwithstanding — did not cease to function in its customary fashion. Indeed, AT&T was unable during the trial to prove *any* actual harm to the network from the elimination of the PCAs.

In its procurement part of the case, the government alleged, and there was proof, that AT&T used its control over the local Operating Companies to force them to buy products from Western Electric even though other equipment manufacturers produced better products or products of identical quality at lower prices. Here, too, AT&T's control of the Operating Companies was central to the allegedly anticompetitive behavior.[137]

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[134] See, *e.g.*, direct and cross examination of Donald H. Erickson (August 6, 1981), Edward Goldstein (August 4, 1981), and William Ellinghaus (August 12, 1981). It should also be noted, however, that, with respect to a number of these problems. AT&T did provide factual explanations of varying degrees of persuasiveness. *Compare* the testimony of Lawrence A. Hohmann (August 24, 1981) *with* that of Robert B. Brunson (August 25, 1981) who was convincing notwithstanding severe cross examination by the government.

[135] Under a certification program, non-Bell equipment may be connected directly to the AT&T network — without the use of a PCA — provided that the equipment has been certified as meeting certain technical standards.

[136] There is some merit to AT&T's claim that it was the FCC, rather than AT&T, that was responsible for the delay in the development of standards. Specifically, although the question of certification as opposed to PCA arose as early as 1968, the FCC did not request technical comments on the standards it had proposed until 1975.

[137] It should be noted, however, that the government's procurement case was not extremely strong. In the first place, it consisted only of sixteen individual "episodes." Measured against the large field of procurement decisions in which the Bell System was engaged, this was not a formidable

Without making definitive findings on any or all of the issues, it is certainly clear that — to the extent that the proposed decree is offered by the government on the premise that it will destroy the basis of past anticompetitive behavior — the Court would not be justified in rejecting it as constituting a remedy for non-existent anticompetitive acts.

2. *Concentration of Power in the Telecommunications Industry*

There is an additional reason, largely independent of the factors discussed above, which supports some type of antitrust relief in this case: AT&T's substantial domination of the telecommunications industry in general.

The antitrust laws are most often viewed as only a means for ensuring free competition in order to achieve the most efficient allocation of society's resources. See pp. 28–29 *supra*. However, Congress and the courts have repeatedly declared that these laws also embody "a desire to put an end to great aggregations of capital because of the helplessness of the individual before them." *United States*. v. *Aluminum Company of America*, 148 F.2d 416, 428 (2d Cir. 1945) (footnote omitted). See also *Standard Oil Co.* v. *United States*, 221 U.S. 1, 50 (1911); *United States* v. *Trans-Missouri Freight Ass'n*, 166 U.S. 290, 323-24 (1897).

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number. It is difficult to evaluate, and the Court will not now evaluate, whether this relative paucity of evidence was due to intrinsic problems of proof when dealing with a company of the size of AT&T, or whether, having conscientiously and carefully surveyed Bell's activities, the government was simply unable to produce more than sixteen questionable episodes because there was no more even arguably anticompetitive activity. Moreover, even as to those sixteen episodes the proof was not overwhelming. Where the government's evidence tended to demonstrate anticompetitive acts, AT&T's market share was generally not high; where market share was high, there was relatively little evidence of anticompetitive acts.

The part of the case dealing with pricing of equipment sold by Western Electric was dismissed on September 11, 1981. See, *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1380-81.

The legislators who enacted the Sherman Act voiced concerns beyond the effects of anticompetitive activities on the economy: they also greatly feared the impact of the large trusts which then dominated the business world on the nation's political system, and they regarded the power of these trusts as an evil to be eradicated. Thus, Senator Sherman stated:

> If the concentrated powers of [a] combination are intrusted to a single man, it is a kingly prerogative, inconsistent with our form of government, and should be subject to the strong resistance of the State and national authorities. If anything is wrong, this is wrong. If we will not endure a king as a political power we should not endure a king over the production, transportation, and sale of any of the necessaries of life.

21 Cong. Rec. 2457 (1890).[138]

These views have been repeatedly echoed since that time, as, for example, during the congressional debates at the time of the enactment of the 1950 amendments to the Clayton Act. See 96 Cong. Rec. 16450 (1950) (Remarks of Sen. Kefauver); 95 Cong. Rec. 11494 (1950) (Remarks of Rep. Bryson); 95 Cong. Rec. 11486 (1949) (Remarks of Rep. Celler). See also *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 344 (1962). As Justice Douglas stated in his dissenting opinion in *United States* v. *Columbia Steel Co.*, 334 U.S. 495, 536 (1948):

> Power that controls the economy should be in the hands of elected representatives of the people, not in the hands of an industrial oligarchy. Industrial power should be decentralized. It should be scattered into many hands so that the fortunes of the people will not be dependent on the whim or caprice, the political prejudices, the emotional stability of a few self-appointed men. The fact that they are not vicious men but respectable and social-minded is irrelevant. That is the philosophy and the command of the Sherman Act. It is founded on a theory of hostility to the concentration in private hands of power

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[138] See also 21 Cong. Rec. 2460, 2569 (1890) (Remarks of Sen. Sherman); 21 Cong. Rec. 2598 (1890) (Remarks of Sen. George).

so great that only a government of the people should have it.[139]

Our political system is designed so that the power of one group may be checked by the power of another. The antitrust laws require this same approach in the economic sphere. Obviously, if one company controlled an essential part of the economy, it would be in a position to gain an undue influence over economic decisions and, as a result, most likely over political decisions. Thus, the antitrust laws seek to diffuse economic power in order to promote the proper functioning of both our economic and our political systems. See generally, A. D. Neale, *The Antitrust Laws of the United States of America*, 422-23 (1962): Blake & Jones, *Antitrust Dialogue: Defense*, 65 Colum. L. Rev. 337, 384 (1965).

The significance of these concepts is accentuated by the context in which the Court must consider the public interest in these cases. The telecommunications industry plays a key role in modern economic, social, and political life. Indeed, many commentators have asserted that we are entering an age in which information will be the keystone of the economy[140] as steel was when Justice Douglas wrote in the *Columbia Steel Co.* case.[141]

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[139] A number of distinguished commentators have challenged this interpretation of the antitrust laws, claiming that the promotion of consumer welfare through ensuing free competition is their sole goal. See R. Bork, *The Antitrust Paradox* 50-89 (1978): 1 P. Areeda & D. Turner, *Antitrust Law, supra* at §§ 103-112. Resolution of this dispute may be crucial when the two objectives point to different solutions. Here, where the remedy necessary to promote free competition is also likely to reduce the concentration of economic power, consideration of the latter would appear to be less controversial. In any event, the cases and the legislative history of the Sherman Act empower the Court to consider broad public interest goals, such as this one, in evaluating the need for an antitrust remedy.

[140] See, *e.g.*, G. Robinson, Ed., *Communications for Tomorrow* (1978).

[141] Commentators from a wide range of the ideological spectrum agree on this conclusion. Thus, Professor Arthur Schlesinger, Jr. has been quoted as stating that "Karl Marx held that history is shaped by control of the means of production; in our times history is shaped by control of the means of communication." T. White, *America in Search of Itself* at 101 (1982). Charles Marshall, AT&T executive vice president, and consumer advocate

The only pervasive two-way communications system is the telephone network. It is crucial in business affairs, in providing information to the citizenry, and in the simple conduct of daily life. In its present form, AT&T has a commanding position in the industry. The men and women who have guided the Bell System appear by and large to have been careful not to take advantage of its central position in America's economic life. There is no guarantee, however, that future managers will be equally careful.[142] In any event, it is antithetical to our political and economic system for this key industry to be within the control of one company.

For these reasons, the Court concludes that the loosening of AT&T's control over telecommunications through the divestiture of the Operating Companies will entail benefits which transcend those which flow from the narrowest reading of the purpose of the antitrust laws.

B. Effect of the Divestiture

The remedy in an antitrust action — whether imposed by a court or agreed upon between the parties — is measured both by how well it halts the objectionable practices and by its prospects for minimizing the likelihood that such practices will occur in the future. See Part II *supra*. Where, as here, the Court has heard substantially all of the evidence, it is appropriate that it weigh the proposed remedy against the evidence in that context.

As indicated in Part IV(A) *supra*, the ability of AT&T to engage in anticompetitive conduct stems largely from its

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Ralph Nader have likewise both noted the displacement of the industrial age by the information age. *Telecommunications Act of 1982: Hearings on H.R. 5158 Before the Subcomm. on Telecommunications, Consumer Protection, and Finance of the House Comm. on Energy and Commerce (Part 2)*, 97th Cong., 2d Sess. 111, 587 (1982).

[142] One may speculate, for example, on the effect on the political life of this nation if a company or group with strong political or ideological opinions were to gain effective control of the present Bell System (particularly if the company, additionally, were not precluded from entry into information and electronic publishing services). See part VI(C) *infra*.

control of the local Operating Companies. Absent such control, AT&T will not have the ability to disadvantage competitors in the interexchange and equipment markets.

For example, with the divestiture of the Operating Companies AT&T will not be able to discriminate against intercity competitors, either by subsidizing its own intercity services with revenues from the monopoly local exchange services, or by obstructing its competitors' access to the local exchange network. The local Operating Companies will not be providing interexchange services, and they will therefore have no incentive to discriminate. Moreover, AT&T's competitors will be guaranteed access that is equal to that provided to AT&T, and intercity carriers therefore will no longer be presented with the problems that confronted them in that area. See Part VIII, *infra*.

Abuses will also be unlikely in the equipment interconnection area, for the simple reason that the Operating Companies will not manufacture equipment and will therefore lack AT&T's incentive to favor the connection of one manufacturer's equipment over another's. Even as to the part of the government's case dealing with procurement, the divestiture of the Operating Companies will go a long way toward eliminating the potential for anticompetitive behavior. Any pro-Western Electric bias on the part of these companies will be eliminated once the intraenterprise relationship between the Operating Companies and Western Electric is broken.[143]

To the extent, then, that the proposed decree proceeds on the assumption that the structural reorganization will make it impossible, or at least unprofitable, for AT&T to engage in anticompetitive practices, it is fully consistent with the public interest in the enforcement of the antitrust laws. The soundness of this remedy becomes even more apparent when it is compared with other relief alternatives.

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[143] Any cross subsidization of AT&T's intercity services and equipment manufacturing operations with revenue from its monopoly local exchange services will likewise be eliminated.

C. Alternative Remedies

In order to determine whether the divestiture proposed by the parties is the remedy which will most effectively fulfill the goals of the antitrust laws, it is appropriate for the Court to evaluate the various alternative remedies that may have been considered or proposed. See 15 U.S.C. § 16(e)(1).

Three alternatives to the divestiture of the Operating Companies emerged in the course of the *AT&T* litigation. The first would have required the divestiture of Western Electric and Bell Laboratories from AT&T.[144] The second, similar in concept if not in detail, would have had as its most salient feature the divestiture from AT&T of portions of Western Electric and Bell Laboratories and of several Bell Operating Companies.[145] The third was a strictly injunctive, non-structural remedy, which would have imposed detailed constraints upon AT&T's activities.[146] None of these alter-

[144] This remedy was first proposed in the government's complaint. See Complaint at 14.

[145] Competitive Impact Statement at 50-51. The Operating Companies retained by AT&T would have been required to provide local telephone service through a separate subsidiary; several other problems would have been dealt with by injunctive provisions.

This proposal was considered by the parties in early 1981, just prior to the start of the trial in the *AT&T* action. At that time, in a successful effort to secure a continuance (see p. 11 *supra*), the parties advised the Court that a concrete settlement had been reached, with no substantive issues remaining to be resolved. See Memorandum Order filed January 16, 1981. However, the Competitive Impact Statement indicates that, to the contrary, no proposal was ever drafted. Competitive Impact Statement at 50.

[146] *Id.* at 51-52. This proposal was discussed by the parties "shortly prior to the negotiations that gave rise to the [present settlement]." *Id.* at 51. It would have required AT&T to grant non-discriminatory access for intercity carriers to the Bell Operating Companies' local exchange facilities, and it would have imposed limits on Western Electric's sales to the Bell System, in addition to limiting the dissemination of information and the rotation of personnel within the Bell System. These injunctive provisions would have been monitored by special masters appointed by the Court.

natives would be as efficacious as the divestiture of the Operating Companies embodied in the proposed decree.[147]

1. *Divestiture of Western Electric and Bell Laboratories*

The divestiture of all or part of Western Electric and Bell Laboratories from AT&T, with or without the divestiture of some, but not all, of the Bell Operating Companies,[148] suffers from several defects in comparison with the parties' present proposal: (1) it would not be as effective in eliminating anticompetitive conduct, and (2) it would have a greater adverse impact on future contributions of the Bell System to the national economy.

The inadequacy of the divestiture from the Bell System of its research and manufacturing arms as an antitrust remedy is obvious: it would not eliminate AT&T's ability and incentive to take anticompetitive actions against its competitors in the intercity market. The remedy would thus be ineffective in the very area in which the government's proof in the *AT&T* action was strongest.[149] In addition, this remedy would not eliminate AT&T's de facto control of the national telecommunications system. Although the company would no longer dominate the manufacturing and research markets, it would still control the essentials of American telecommunications — virtually all intercity and local services. The divestiture would thus not fulfill the goal of deconcentrating AT&T's vast economic power.

The divestiture of Western Electric and Bell Laboratories would suffer from an additional defect. Considerable evidence

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[147] The Court's evaluation of these remedies is conducted strictly in the context of its decision on the adequacy of a negotiated settlement. If the *AT&T* action were to proceed to final judgment and liability were found, the Court might determine that the measures discussed in this segment of the opinion are appropriate remedies, either as alternatives to the divestiture of the Operating Companies or in addition to such divestiture.

[148] Because of their conceptual similarities, the first and second alternate remedies are being discussed together.

[149] The additional divestiture of several Bell Operating Companies would remedy this problem only as to the areas served by these divested companies.

was adduced during the *AT&T* trial concerning the central role of Bell Laboratories — and to a lesser degree of Western Electric — in innovation in the telecommunications industry and, more broadly, in industrial research.[150] AT&T argued vigorously that the present structure of the Bell System was in significant part responsible for this admirable record because the researchers were linked with a manufacturer — Western Electric — and with two service organizations — the Operating Companies and the Long Lines Department.[151]

The Court is of the opinion that there is considerable merit to these contentions. Bell Laboratories has been a positive force both in basic and in applied research, and this research has had a beneficial effect on the nation's economic position in all of its varied aspects.[152] It also seems to be true that the links between Bell Laboratories and the manufacturing and service arms of the Bell System have been of assistance in the achievement of these technological successes.

On this basis, then, the separation of Bell Laboratories from all of these functions could have an adverse effect upon future research and development,[153] and it may for that reason be regarded as less desirable than the present proposal which would leave Bell Laboratories associated with a manufacturer and two service organizations — Long Lines and AT&T's new information services — which would supply the practical experience that would be useful in stimulating the research operations.

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[150] Testimony of Solomon Buchsbaum (September 23, 1981); testimony of Edward E. David, Jr. (November 4, 1981); testimony of David Packard (November 6, 1981); see also Exhibit D-1-134.

[151] Testimony of Morris Tanenbaum (September 8, 1981); testimony of William D. Nordhaus (November 5, 1981); testimony of Bruce C. Netschert (November 12, 1981); testimony of Paul R. Lawrence (November 6, 1981); testimony of Nathan Rosenberg (November 10, 1981).

[152] This includes basic scientific advance, cheaper and better products for consumers, foreign trade, and national defense.

[153] In light of AT&T's agreement to divest the Operating Companies, the predictions made by a number of eminent witnesses regarding the dire consequence certain to follow from such divestiture appear in retrospect to have been vastly overrated.

2. *Injunction*

The second major alternative to the proposed decree is an injunction which would be enforced by special masters appointed by and responsible to the Court. This alternative, too, suffers from a number of defects.

It would be difficult to formulate an order that would effectively deal with all of the different kinds of anticompetitive behavior that are claimed to have occurred over a considerable period of time, in various geographical areas, and with respect to many different subjects. There is evidence which suggests that AT&T's pattern during the last thirty years has been to shift from one anticompetitive activity to another, as various alternatives were foreclosed through the action of regulators or the courts or as a result of technological development.[154] In view of this background, it is unlikely that, realistically, an injunction could be drafted that would be both sufficiently detailed to bar specific anticompetitive conduct yet sufficiently broad to prevent the various conceivable kinds of behavior that AT&T might employ in the future.[155]

An even more formidable obstacle is presented by the question of enforcement. Two former chiefs of the FCC's Common Carrier Bureau, the agency charged with regulating AT&T, testified that the Commission is not and never has been capable of effective enforcement of the laws governing

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[154] It is claimed, for example, that after the legal defense against interconnection of non-Bell equipment became impossible to sustain, AT&T shifted to claims that inferior equipment was being produced by non-Bell manufacturers; alleged that harms to the network would result from such equipment; and sought regulation by state as distinguished from federal agencies, and the like. See Plaintiff's Memorandum in Opposition to Defendants' Motion for Involuntary Dismissal in the *AT&T* action at 296-359.

[155] For these reasons, and because of the enforcement problems discussed below, courts have generally rejected this type of detailed injunction in favor of the "surer, cleaner remedy of divestiture." *United States* v. *E. I. duPont de Nemours & Co.*, *supra*, 366 U.S. at 334. See also *United States* v. *Paramount Pictures, Inc.*, 334 U.S. 131, 165-75 (1948); *United States* v. *Crescent Amusement Co.*, *supra*, 323 U.S. at 189-90.

AT&T's behavior.[156] In their view, this inability was due to structural, budgetary, and financial deficiencies within the FCC as well as to the difficulty in obtaining information from AT&T. Whatever the true cause, it seems clear that the problems of supervision by a relatively poorly-financed, poorly-staffed government agency over a gigantic corporation with almost unlimited resources in funds and gifted personnel are no more likely to be overcome in the future than they were in the past.[157]

These difficulties would be exacerbated if enforcement of a broad injunction were vested in court-appointed special masters. To be sure, such officials have proved in the past to be capable of performing relatively narrow, short-term responsibilities, and to perform them well. But the type of broad injunctive relief that would be needed in these cases would require quasipermanent supervision of all of AT&T's activities by not one or two special masters but by a vast staff. In short, what would be required would be a re-creation of the FCC's Common Carrier Bureau in the guise of an arm of the Judiciary. Such a development would be undesirable for many different reasons.[158] Furthermore, there is no reason to believe that, in the end, a judicially-created bureaucracy would be any more capable than the FCC itself of performing the unending task of vigilance and oversight that would be required to ensure that an integrated Bell System did not engage in anticompetitive conduct.

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[156] Testimony of Walter Hinchman (June 18, 1981); testimony of Bernard Strassburg (October 14, 1981). Other persons with expertise in telecommunications regulation expressed similar views. Testimony of William Melody (June 8, 1981); testimony of Nina Cornell (June 19, 1981); testimony of Bruce Owen (June 22, 1981).

[157] Recent developments in governmental policy point to a further reduction in the funding, the authority, and hence the effectiveness of regulatory agencies such as the FCC.

[158] From a philosophical point of view, such a remedy could contravene the separation of powers doctrine because it would involve the creation of a substantial quasi-legislative, quasi-executive bureaucracy within the Judicial Branch of the government. Practically, the remedy could be impossible to administer because of the need for substantial budgetary authority and a large administrative apparatus.

D. Effect of the Divestiture Upon Other Interests

A number of individuals have written to the Court and to the Department of Justice urging the rejection of the proposed decree. They contend that AT&T in its present, integrated form has rendered excellent and affordable telephone service to the citizens of this nation, including those with modest incomes and those who live in sparsely populated areas. Many note that AT&T's securities have been a mainstay of the small investor, with a long history of stable prices and dividend payments. Given that record, the argument goes, the break-up of AT&T could not possibly be in the public interest. While the Court has very carefully considered these concerns,[159] it has concluded that they are not sufficient to overcome the considerations supporting divestiture.

The divestiture of the Operating Companies will not necessarily have an adverse effect upon the cost of local telephone service.[160] The decree would leave state and federal regulators with a mechanism — access charges — by which to require a subsidy from intercity service to local service. By means of these access charges, the regulators are free to maintain local rates at current levels or they may so set the charges as to increase or decrease local rates.[161]

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[159] Careful consideration and independent analysis have been particularly appropriate because these objections were primarily voiced by individual citizens who lacked the resources to present detailed briefs.

[160] There is a dispute, reflected at the trial as well as in other forums, over the question whether local telephone service has ever actually been subsidized by intercity service as AT&T has consistently claimed. See Testimony of John D. deButts (August 27, 1981); testimony of William J. Baumol (December 7, 1981). The government contended that, to the contrary, local telephone revenues have subsidized AT&T's intercity rates (see Testimony of William H. Melody (June 8, 1981); testimony of Nina Cornell (June 19, 1981); testimony of Bruce Owen (June 22, 1981)) and since the trial was aborted by the settlement, no final decision was reached on this issue.

[161] Although the decree requires the Operating Companies to file "cost justified" tariffs for access charges, it leaves to the regulators the decision as to what costs should be included within this calculation. Department of Justice Response to Comments at 106-107; AT&T Reply Brief at 22-23. If the regulators chose to retain the cost allocation presently used in the

As to the second claim, there is simply no evidence or reason to believe that, funding aside, the quality of service will decline as a result of divestiture. The divested Operating Companies will not be technical backwaters: they will have substantial incentives to upgrade their networks and to provide high-quality interconnections for other carriers in order to maximize revenues from access charges and from local rates.

As noted above, it is unlikely that the divestiture will impair the research capabilities of Bell Laboratories. See pp. 61–62 *supra*. The scientists and engineers working in that organization will retain their incentive to improve the equipment and technology used to provide local telephone service, if only because the largest potential customers of Western Electric — Bell Laboratories' companion in the "new" AT&T complex — will be the divested Operating Companies.[162] In addition, AT&T's information services and interexchange services can be provided to customers only over the Operating Companies' facilities, again creating large incentives for continued improvement and upgrading of these facilities.[163]

In the final analysis, it is apparent that, as with so many public issues, a choice must be made.

There has long been a debate over the relative merits of

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separations and settlements process, the subsidy from interexchange revenues to local rates will remain at current levels. Under the proposed decree, state regulators will set access charges for intrastate interexchange service and the FCC will set access charges for interstate interexchange service. Department of Justice Response to Comments at 106-107; AT&T Reply Brief at 22-23. If a subsidy is required beyond that implicit in the access charges, it may be provided by state or federal legislation. See, *e.g.*, H.R. 5158, 97th Cong, 2d Sess. § 234 (proposal for a National Telecommunications Fund).

[162] Indeed, their incentive may be even greater after divestiture than it was before, since after divestiture Western Electric will have lost its anticompetitive advantage and will instead be forced to compete with other manufacturers on the basis of quality and price for the Operating Companies' business.

[163] The concerns of investors are similarly unfounded. They will retain all their legal remedies for any improper actions by AT&T in connection with the divestiture. See Part IX *infra*.

regulation and competition. The evidence adduced during the *AT&T* trial indicates that the Bell System has been neither effectively regulated nor fully subjected to true competition. The FCC officials themselves acknowledge that their regulation has been woefully inadequate to cope with a company of AT&T's scope, wealth, and power. The efforts of various arms of government to introduce true competition into the telecommunications industry have been similarly feeble. The antitrust suit brought by the Department of Justice in 1949 ended in 1956 with a consent decree which imposed injunctive relief that was patently inadequate. It took from 1968 when the *Carterfone* decision[164] was handed down by the FCC to 1978 when the United States Court of Appeals decided *Execunet II*[165] to establish even the very principle of competition so that it was beyond dispute. Future regulatory and injunctive remedies are unlikely to be more successful than were similar efforts in the past. In short, the choice is between a Bell System restrained by neither regulation nor true competition and a Bell System reorganized in such a way as to diminish greatly the possibility of future anticompetitive behavior.

The history of the American economic system teaches that fair competition is more likely to benefit all, especially consumers, than an industry dominated by a single-company monopolist. There is no reason to believe that the experience of the telecommunications industry will be contrary to that rule.

For all of these reasons, the Court concludes that the divestiture from AT&T of companies providing local telephone service is in the public interest.

## V

## Absence of Restrictions on AT&T

Under the terms of the proposed decree, the line of business restrictions and the licensing requirements imposed by the

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[164] 13 F.C.C.2d 420 (1968).

[165] *MCI Telecommunications Corp.* v. *FCC*, 580 F.2d 590 (D.C. Cir. 1978).

1956 consent decree in the *Western Electric* case would be removed and AT&T would be free to compete in all facets of the marketplace.[166] Some of the opponents of the proposed decree argue that several of the restrictions contained in the 1956 decree should not be eliminated, and others contend that the Court should also impose additional restrictions, not present in the 1956 decree. For the reasons explained in this part of the opinion and Part VI below,[167] the Court finds that, with one exception (see Part VI(B) *infra*), the imposition of restrictions on AT&T would not be in the public interest.

The antitrust laws do not require that a company be prohibited from competing in a market unless it can be demonstrated that its participation in that market will have anticompetitive effects. Past restrictions on AT&T were justified because of its control over the local Operating Companies. With the divestiture of these local exchange monopolies, continued restrictions are not required unless justified by some other rationale.

A. AT&T Power in the Interexchange Market

Virtually all those who suggest that restrictions beyond those in the proposed decree be imposed on AT&T make the same general arguments. Their basic claim is that AT&T still possesses monopoly power in the interexchange market[168] and that it will leverage this power by cross subsidizing its competitive services with monopoly revenues.[169] These interexchange monopoly revenues, it is said, will subsidize a

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[166] The only limitation regarding AT&T's business activities is that it may not reacquire the Operating Companies.

[167] This part of the opinion considers general restrictions on AT&T; Part VI deals with restrictions on the provision of information services.

[168] See Part V(C) for a discussion of the claim that AT&T has monopoly power in the equipment manufacturing market.

[169] In addition to advancing the cross-subsidization argument, those who advocate restrictions on AT&T also raise contentions based on discrimination. However, because these discrimination claims take on a variety of forms dependent on the context, the Court will address them in its discussion of the specific restrictions that have been proposed.

variety of business activities, ranging from competitive interexchange routes to equipment manufacturing to alternative local distribution facilities.

The validity of these arguments depends, of course, upon the soundness of the claim that after the divestiture AT&T will still possess monopoly power in the interexchange market. If AT&T lacks such power, it would be unable to reap supracompetitive profits with which to support its other activities; it would only recover a profit commensurate with its interexchange operations.

There can be no doubt that AT&T's market share in the interexchange market is high. Although it is not possible to focus on a precise figure inasmuch as the number of market share estimates is almost as varied as the number of persons submitting comments, even AT&T concedes that as late as 1981 its share of interexchange revenue was around 77 percent.[170] But the inquiry of whether AT&T possesses monopoly power in the interexchange areas does not end with a description of AT&T's size or its market share.

As defined by the Supreme Court, monopoly power is "the power to control prices or exclude competition." *United States* v. *Grinnell Corp.*, *supra*, 384 U.S. at 571 (1966); *United States* v. *duPont & Co.*, 351 U.S. 377, 391 (1956). Although monopoly power may be inferred from a firm's predominant share of the market, size alone is not synonymous with market power, particularly where entry barriers are not substantial. *United States* v. *Grinnell*, *supra*, 384 U.S. at 571; *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1347; Posner, *Market Power in Antitrust Cases*, 94 Harv. L. Rev. 937, 947-51 (1981).

Both the Department of Justice and AT&T contend that competition in the interexchange market is growing and that

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[170] Estimates submitted by others were significantly higher, some contending that AT&T's market share exceeds 90 percent. It is unnecessary for purposes of this proceeding to resolve the conflict, for the precise amount of the market share is not decisive to the Court's holding.

this increase in competition demonstrates an absence of monopoly power.[171] There is some validity to this claim. The interexchange market is now being served not only by relatively young businesses but also by subsidiaries of such well established firms as ITT, Southern Pacific, and IBM.

That is not to say, however, that competition has flourished without impediment or that it would soar if the Bell System were not broken up. There is substantial merit in the suggestion that, absent divestiture, AT&T would still possess significant monopoly power, and that whatever competition developed in the past did so despite anticompetitive conditions. See Part IV *supra*. But the overriding fact is that the principal means by which AT&T has maintained monopoly power in telecommunications has been its control of the Operating Companies with their strategic bottleneck position. The divestiture required by the proposed decree will thus remove the two main barriers that previously deterred firms from entering or competing effectively in the interexchange market.

First. AT&T will no longer have the opportunity to provide discriminatory interconnection to competitors. The Operating Companies will own the local exchange facilities. Since these companies will not be providing interexchange services, they will lack AT&T's incentive to discriminate. Moreover, they will be required to provide all interexchange carriers with exchange access that is "equal in type, quality, and price to that provided to AT&T and its affiliates." Proposed Decree, Section II. See Part VIII *infra*.

Second. Once AT&T is divested of the local Operating Companies, it will be unable either to subsidize the prices of its interexchange service with revenues from local exchange services or to shift costs from competitive interexchange services.

With the removal by the decree of all these burdens on competition, the number of firms entering the interexchange

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[171] The Department took a contrary position during the *AT&T* trial.

market is thus likely to increase.[172] This development should be further assisted by the reduction of other barriers to entry. For example, although the cost of entering the telecommunications business is still substantial, the size of the required capital investment is not as great as it once was.[173] In addition, as more competitors begin to offer more services that are comparable to those offered by AT&T,[174] entrenched customer preferences in favor of AT&T will decrease.

With the removal of these barriers to competition, AT&T should be unable to engage in monopoly pricing in any market. To be sure, there are a number of routes for which AT&T is

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[172] It must be remembered that the regulatory decisions which introduced competition into the interexchange market are themselves relatively recent. It was not until 1978 that the provision of regular long distance telephone service (*i.e.*, MTS/WATS type service) became subject to competition. For a survey of the decisions leading to full competition in the interexchange market, see Docket 11866, *Allocation of the Frequencies in the Bands Above 890 Mc.*, 27 F.C.C. 359 (1959); Docket 16509, *Microwave Communications, Inc.*, 18 F.C.C.2d 953 (1969), 21 F.C.C.2d 190 (1970); Docket 18920, *Specialized Common Carriers*, 29 F.C.C.2d 870 (1971), *aff'd sub. nom. Washington Utilities and Transportation Commission* v. *F.C.C.*, 513 F.2d 1142 (9th Cir. 1975); Docket 16495, *Establishment of Domestic Communications Satellite Facilities by Non-Governmental Entities*, 35 F.C.C.2d 844 (1972); *MCI Telecommunications Corp.* v. *FCC*, 561 F.2d 365 (D.C. Cir. 1977) (*Execunet I*); *MCI Telecommunications Corp.* v. *F.C.C.*, 580 F.2d 590 (D.C. Cir. 1978) (*Execunet II*). The FCC decisions allowing interexchange carriers to expand their service offerings by reselling and sharing AT&T services have likewise been in force only for the last several years. *Regulatory Policies Concerning Resale and Shared Use of Common Carrier Services*, 60 F.C.C.2d 261 (1976), *reconsidered*, 62 F.C.C.2d 588 (1977), *aff'd. sub. nom. AT&T* v. *F.C.C.*, 572 F.2d 17 (2d Cir. 1978); *Regulatory Policies Concerning Resale and Shared Use of Common Carrier Domestic Public Switched Network Services*, Docket No. CC 80-54, 83 F.C.C.2d 167 (1981).

[173] This reduction in the amount of capital investment is due in part to the development of new technologies, such as satellites and microwave towers, and in part to the recent regulatory decisions allowing for the resale and sharing of AT&T services. See note 172, *supra*.

[174] See, e.g., *MCI* v. *FCC*, 561 F.2d 365 (D.C. Cir. 1977); *MCI* v. *FCC*, 580 F.2d 590 (D.C. Cir. 1978); *MTS & WATS Market Structure*, CC Docket 78-72, Report & 3rd Supplemental Notice of Inquiry and Proposed Rulemaking, 81 F.C.C.2d 177 (1980).

the sole interexchange carrier. However, several of these routes serve sparsely populated areas and are only marginally profitable. On the other hand, should it turn out that these routes are in fact lucrative and that AT&T is nevertheless charging monopoly prices, then, following divestiture, market forces should fairly rapidly remedy the situation: because of the elimination of entry barriers, new entrants will be attracted to these markets, and prices, in turn, will fall to their competitive levels.

For these reasons, it appears that after divestiture, AT&T will largely lack the monopoly power that the opponents of the decree suggest,[175] and the trend of increasing competition may therefore be expected to continue.[176]

Thus, unless proposed restrictions on AT&T are premised on more than the claim that AT&T has monopoly power in the interexchange area, they will have to be rejected.

B. Interexchange Restrictions

Some of those who have commented on the proposed decree[177] urge that the Court require a modification which would add a clause guaranteeing access to AT&T's interexchange network for its competitors, and another which would require AT&T's Long Lines Department to be placed in a fully separated subsidiary. The imposition of such modifications is not warranted.

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[175] The Court does not find that there is *no* possibility that AT&T will use its still considerable market share in an anticompetitive manner. It does find, however, that for the reasons cited, both the incentive and the opportunity for anticompetitive conduct will after divestiture and on account of divestiture be greatly reduced.

[176] To the extent that AT&T still has some potential for engaging in anticompetitive behavior, there is of course nothing in the proposed decree to immunize it from its obligations under the regulatory decisions or the antitrust laws.

[177] Most of those who have submitted briefs or comments — including AT&T's most major interexchange competitors (*e.g.*, MCI Corp.) — either did not address the subject of restrictions on AT&T at all or they agreed with the decree's provisions as drafted.

Those who argue for these restrictions essentially cite no reason other than AT&T's share in the interexchange market to support their demands and, as discussed *supra*, that alone is insufficient.

Additionally, the proposed restrictions are substantively deficient. As the proponents of a clause which would guarantee access to AT&T's interexchange competitors concede,[178] such access is already required by existing FCC decisions and regulations. These regulations make it possible for competing carriers to interconnect freely and to expand their facilities by "piecing out" AT&T's network, that is, by using AT&T's facilities to complete portions of routes that must traverse low density, sparsely populated, and hence presumably not very profitable territory. See note 172 *supra*. There is no basis for simply repeating in the decree[179] precisely that which is already contained in the FCC regulations.

The second proposed restriction — that Long Lines be placed in a separate subsidiary — is likewise unsupported either by necessity or by adequate reasoning. This restriction is required, it is said, to prevent AT&T from using its interexchange revenues to subsidize its competitive services. But as the Court has stated elsewhere (see Part VII *infra*), if cross subsidization is a problem, a separate subsidiary will not resolve it. Moreover, AT&T's opportunity for any cross subsidization will become increasingly curtailed as interexchange competition increases; excessive profits from that service with which to subsidize other activities would quickly

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[178] *E.g.*, Topic 3 briefs submitted by Association of Data Communications Users and the Utilities Telecommunications Council at 11; Mobile Marine Radio Inc. at 10; and Satellite Business Systems at 17.

[179] Such duplication might actually have its drawbacks, for it would make it impossible to alter the present requirements should they no longer appear to be in the public interest; (*i.e.*, should the FCC find that, because conditions had become more competitive, the present interconnection requirements are no longer warranted). With the divestiture of the Operating Companies, regulation of interexchange services will in all probability become more effective since AT&T will no longer be able to shift costs in the manner that the government has alleged it has done in the past.

attract lower-priced competitors into the interexchange field or stimulate existing competitors into expanding their networks to displace AT&T.

For these reasons, the proposed interexchange restrictions must be rejected.

C. Equipment Restrictions

The restrictions that are suggested in the area of equipment manufacturing are of three basic types: that AT&T's equipment manufacturing and marketing operations be placed in a separate subsidiary or even, in the view of some of those who submitted comments, divested;[180] that AT&T be required to disseminate its network standards and technical information; and that procurement quotas be imposed on the Operation Companies and on AT&T's Long Lines Department.

In addition to justifying these restrictions on the basis discussed above — that is, on AT&T's interexchange market share — their proponents support their position on two other grounds: that AT&T possesses monopoly power in the equipment market, and that the association with Bell Laboratories and Long Lines provides Western Electric with anticompetitive advantages in the manufacturing of equipment. The Court will examine each of the arguments in turn.

There is no merit to the claim that after divestiture AT&T will possess monopoly power in the area of equipment manufacturing. In reviewing the proof on anticompetitive behavior in the equipment market — even before divestiture — the Court found that the government's evidence on that aspect of the case was less convincing than, for example, on that involving intercity services. As explained in Part IV *supra*, where the government was able to show that AT&T's market share was high, it was generally unable to demonstrate significant anticompetitive behavior; where evidence of behavior was more damning, it had difficulty establishing market power. Thus, at a minimum the factual predicate for drastic

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[180] Additional reasons for a rejection of this proposal are discussed in Part IV *supra*.

restrictions in the equipment area is not as apparent as it might be with respect to other subjects.

After divestiture, AT&T's position in the equipment market will be further diminished, and that market is certain to become more competitive.[181] To the extent that prior to divestiture AT&T was able to engage in anticompetitive conduct in the equipment market, that ability stemmed basically from its control of the Operating Companies. Once these local companies are divested, Western Electric will lose its captive customers. Not only does the proposed decree eliminate the Operating Companies' intra-enterprise incentive to purchase Western Electric equipment, but it also includes specific provisions that prohibit these companies from discriminating in the procurement of equipment. One of these provisions requires that within six months after the reorganization of AT&T, each Operating Company must submit to the Department of Justice compliance procedures explaining how that company plans to carry out its equipment procurement obligations. Proposed Decree, Sections II(B) and (C). If an Operating Company discriminates in procuring equipment, that act will constitute a violation of the decree, and an enforcement action may be brought against it.

There is likewise no merit to the argument that Western Electric will have an anticompetitive edge in the production of new equipment because its affiliation with Bell Laboratories and Long Lines will give it early access to technical information and network standards. This claim ignores the fact that after divestiture, the Operating Companies, not AT&T, will control the information necessary for local exchange and exchange access services. Thus, if equipment manufacturers need information about interconnecting their equipment to

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[181] In the interexchange equipment market, for example, Western Electric has a variety of competitors which produce switches and microwave equipment. In the area of equipment manufacturing for computers and computer-related services, far from being the dominant firm, Western Electric will be a new entrant forced to compete with well established domestic and foreign firms.

the local exchange network, it will be provided by companies that are not engaged in the manufacturing of equipment.[182]

There is no competitive basis, therefore, for imposing any of the proposed restrictions on AT&T in the area of equipment manufacturing and marketing.[183]

D. Bypass

A considerable number of persons[184] have suggested that the Court prohibit AT&T from using new local distribution technologies that would allow it to "bypass" the networks of the Operating Companies to reach its local subscribers directly.[185] The fear is that, early on, use of this technology will tend to exert pressure on Operating Companies rates and their ability to levy access charges on interexchange carriers, and that, in time, the new technology will render the Operating Companies and their plant obsolete.

The suggestions for a modification to prohibit bypass would be worthy of implementation only if two premises were

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[182] To the extent that manufacturers need information from Long Lines, market forces will help to ensure their access: since Long Lines will increasingly be forced to compete with other interexchange competitors, it will have the incentive to purchase the best equipment at the lowest prices without regard to corporate affiliation. It will therefore be in Long Line's own interest to disseminate its own technical information and standards as broadly as possible to enable it to choose among the widest range of products. Finally, as technology in interexchange services advances and carriers turn increasingly to the use of microwave towers and satellites, reliance on the AT&T network will decline and the need for obtaining information about the AT&T network will increasingly be reduced.

[183] Far from enhancing competition, the establishment of quotas would produce anticompetitive results: the Operating Companies and Long Lines would be precluded from making purchasing decisions on the basis of quality and price.

[184] Including the members of the House Telecommunications Subcommittee of the House Committee on Energy and Commerce who wrote to the Court on July 27, 1982. See note 63 *supra*.

[185] Initially, this capacity would presumably be used primarily to connect to high-volume users; eventually the bypass technology may permit interconnection to all subscribers.

accepted: (1) that if AT&T does not develop the technology required for bypass, it will not be developed by anyone, and (2) that it is desirable as a matter of public policy to curtail this technological development. Neither premise is well taken.

AT&T is not the only carrier to possess the technical know-how necessary for bypassing the Operating Companies' local networks. Imposition of this restriction on AT&T is thus unlikely to be effective.[186] Furthermore, because other inter-exchange carriers possess this technology, to prohibit only AT&T from developing and using it would artifically and unfairly restrict competition — an action antithetical to the purposes of the antitrust laws.[187]

Even if the Court, by a simple modification of the decree, could stop bypass technology from developing, it would not be justified in doing so. This technology is a threat to the Operating Companies presumably because, when it is developed, it will be more advanced and less expensive than the present method of transmission which depends upon a cumbersome system of poles and wires. Bypass would provide telecommunications service directly to the subscriber by means of satellites, microwave towers, or other advanced technological innovations at a lower cost than such service is available now. If indeed this should prove to be the case — there is general agreement that truly large-scale use of bypass technology is still some time into the future — the answer is not to call a halt to these developments but to make certain

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[186] Indeed, the protection afforded by a ban on AT&T alone would probably be minimal because it is the carrier least likely to exploit the new technology to the fullest inasmuch as its facilities were designed to interconnect with those of the Operating Companies. Moreover, there is a safety valve against overreaching: before AT&T, or any other carrier, may install the facilities necessary to connect directly to the ultimate customers, it must secure approval from the state regulators. If these regulators find for public interest reasons unrelated to competition that bypass should be prohibited, they may do so irrespective of the decree in these cases.

[187] To the extent that the local exchange facilities constitute monopoly bottlenecks, the development of alternative facilities actually furthers the competitive purposes of these laws.

that the benefits will not be distributed in such a way as to undermine the goal of universal service.

Neither the Court nor those who object to the decree can halt the electronic revolution any more than the Luddites could stop the industrial revolution at the beginning of the last century. If and when bypass technology becomes technically and economically feasible for widespread use, it should have the effect of reducing telephone costs and charges across the board, to the benefit of consumers, the economy, and the nation. Should it turn out instead that, as some fear, this technology will be used to reduce charges unevenly so as to threaten the goal of universal service, then those with legislative authority may at that time wish to take steps, through a program of subsidies, special charges, or other regulatory means, to make the benefits of the new technology available to all, including those who are relatively low-volume users of telephone service. But there is no warrant for preventing the development of this technology through a ban on its use by AT&T or otherwise.

E. Patent Licensing Requirements

Under the terms of the 1956 consent decree, AT&T was required to grant to all applicants non-exclusive licenses for all existing and future Bell System patents. 1956 Consent Decree, Section X. In addition, the decree requires that, upon the payment of reasonable charges, AT&T must furnish to those with licenses for AT&T patents the technical information necessary to manufacture the equipment for which the applicant obtained the patent license. Section XIV. These licensing requirements[188] would be eliminated by the proposed decree, and the Court must determine whether such elimination is in the public interest.

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[188] The proposed decree does nothing to affect existing licensing contracts, most of which last for the life of the patent and contain provisions for the licensing of related new patents issued within five years of the execution of the contract. In addition, licenses held by the Operating Companies may be sublicensed to others.

A prime reason for the imposition of the mandatory licensing requirement in 1956 was AT&T's anticompetitive hold on telecommunications and electronics technology.[189] But this technology has advanced rapidly since then, and has become much more widely dispersed, so that AT&T now faces significant challenges in research and development both from established domestic firms and from powerful foreign competitors. The need for continued compulsory licensing of patents, therefore, is diminished on this basis alone.

Divestiture of the Operating Companies may be expected vastly to accelerate this trend. Until now, AT&T's research and development have been financed primarily through the licensing contracts with the local Operating Companies. As long as rate-payer-financed local exchange revenues were supporting this research and development, it made sense to require AT&T to share the fruits of its monopoly financing with others. But under the proposed decree, the licensing contracts will be terminated, and this rationale for exclusive licensing thus falls.

Moreover, AT&T would be forced after divestiture to fund its research and development just like other competitive enterprises — without an artificial subsidy from captive ratepayers. That being so, unless compulsory licensing is eliminated, AT&T would be placed at a significant disadvantage vis-a-vis its competitors: of all those who would be active in the development of new technology, it alone would be compelled to furnish its patents to those who might be interested,[190] including all of its domestic and foreign competitors.[191]

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[189] The complaint in the *Western Electric* action alleged that AT&T engaged in anticompetitive behavior in licensing its own patents and in acquiring the patents of others as part of its efforts to monopolize the telecommunications equipment market. *United States* v. *Western Electric*, *supra*, Complaint at 18–19. The 1956 consent decree contains no finding of patent abuse, but simply states that the terms of the judgment are consented to "without . . . constituting any evidence or admission by any party in respect of any such issues." 1956 Consent Decree at 1.

[190] At the same time, AT&T's new-found need to finance its research and development like other competitive firms will exert some pressure on it to

Some of AT&T's competitors contend next that compulsory licensing is necessary to ensure that equipment manufacturers and interexchange carriers receive the interface information necessary to interconnect with the local exchange network. There is no basis for such claims. As stated in Part V(C) *supra*, after the divestiture, the local Operating Companies, not AT&T, will possess and generate the information necessary for interconnection. The proposed decree requires AT&T to provide these Operating Companies with, *inter alia*, sufficient technical information to permit them to perform their exchange telecommunications and exchange access functions. Proposed Decree, Section I(A)(1). The Operating Companies, in turn, are prohibited from discriminating in the "establishment and dissemination of technical information and procurement and interconnection standards." Section II(B)(2).[192] And since the Operating Companies will neither manufacture equipment nor provide interexchange services, they will have no incentive to favor Western Electric or Long Lines to the detriment of other intercity service providers and equipment manufacturers.

For these reasons, the Court concludes that the provisions in the proposed decree which would eliminate the patent licensing provisions imposed in 1956 are not inconsistent with the public interest.[193]

Somewhat different considerations apply to licensing relationships between AT&T and the local Operating Companies.

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license its patents to others so that, reciprocally, it may receive patents and technical information from them.

[191] Indeed, this disadvantage could discourage AT&T from spending funds for research and development. The resulting diminution of Bell Laboratories' research effort would not be in the public interest. See Part IV *supra*.

[192] In addition, the FCC requires the Operating Companies to make available network interface information necessary for interconnection. See, *e.g.*, 47 C.F.R. § 68.110.

[193] Should AT&T misuse its patents — for example by improperly refusing to license them — the aggrieved parties would be free to pursue their remedies under the patent and antitrust laws: there is nothing in the decree to diminish any of these rights and remedies.

These companies have not only relied on the research of Bell Laboratories; through the licensing contracts they have provided direct financial support for that research. In addition, access to the patents and technical information owned by AT&T is necessary if the Operating Companies are to perform properly their exchange telecommunications and access functions. For these reasons, the Court would be reluctant to approve the proposed decree were the Operating Companies to be spun off without patent and research resources. That, however, is not the case.

Under the terms of the proposed decree, the Operating Companies must be given the technical information needed to perform their functions. Proposed Decree, Section I(A)(1).[194] As part of its compliance with this requirement, AT&T has proposed granting to the Operating Companies on a royalty-free basis, all existing patents and all patents issued for a period of five years following approval of the proposed decree. See, *e.g.*, AT&T Reply Comments at 123. AT&T has also agreed to provide the Operating Companies with non-patentable technical information that has been funded by the license contracts. Specifically, it has stated (AT&T Reply Comments at 123–34, n. **):

> To the extent License Contract work in progress upon the date of divestiture yields useful technical information thereafter, such information shall also be made available to the BOCs for an appropriate period after divestiture. In addition, technical information concerning Western Electric products and systems will be made available to the extent necessary for the BOCs to procure, or otherwise contract for, compatible equipment and systems from other manufacturers.

Finally, the parties have assured the Court that the Operating Companies will have the right to sublicense the AT&T patents and technical information to those providing them with goods

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[194] In addition, until September 1, 1987, the Operating Companies may call upon AT&T, Western Electric, and Bell Laboratories to provide "on a priority basis all research, development, manufacturing, and other support services." Proposed Decree, Section I(C).

and services. See, *e.g.*, Department of Justice Response to Comments at 38–39.

These representations are adequate to support the conclusion that the Operating Companies will possess the necessary patent and technical information resources. The assurances must, of course, be implemented by means of appropriate details in the reorganization plan, and when that plan is submitted pursuant to the procedures set forth in Part XI *infra*, the Court will evaluate these details to make certain that they conform to the general principles implied by these assurances.

## VI

## The 1956 Decree and Line of Business Restrictions

The basic agreement embodied in the 1956 consent decree in the *Western Electric* case[196] was that AT&T would not be required to divest itself of Western Electric, provided that AT&T would restrict its operations to the provision of common carrier communications services[196] and that Western Electric would manufacture only the types of equipment used by the Bell System.[197]

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[196] See Part I *supra*.

[196] Section V of the 1956 decree provides,

> [t]he defendant AT&T is enjoined and restrained from engaging, either directly, or indirectly through its subsidiaries . . . in any business other than the furnishing of common carrier communications services; provided, however, that this Section V shall not apply to . . . businesses or services incidental to the furnishing by AT&T or such subsidiaries of common carrier communications services.

Under Section II(i) of the 1956 decree, common carrier communications services are defined as "communications services and facilities, . . . the charges for which are subject to public regulation under the Communications Act of 1934."

[197] Section IV of the 1956 decree states that

> [t]he defendants are each enjoined and restrained from commencing, directly or indirectly, to manufacture for sale or lease any equipment which is of a type not sold or leased . . . to Companies of the Bell System, for use in furnishing common carrier communications services.

The decree which has now been submitted by the parties would eliminate all of the restrictions of the 1956 consent judgment. If that decree is entered by the Court, AT&T would be free to enter the computer market as well as to provide the full range of so-called information services.[198]

There has been no serious opposition to the entry of AT&T into manufacturing and marketing of computers and other electronic equipment, and there is no question that this

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[198] Although the Court need not at this juncture decide the question whether AT&T could provide any of these information services were the 1956 consent decree to remain in effect, it would appear that, unless that decree is vacated, AT&T would be precluded from offering most, if not all, of these services. Specifically, it is difficult to imagine how the Court could find either (1) that the provision of computer services or electronic news services in competition with others satisfies the 1956 decree's requirements that AT&T provide only common carrier communications services the charges for which are subject to public regulation under the Communications Act or (2) that these services are "incidental" to the furnishing of common carrier communications services.

Similarly, it appears that under the 1956 decree, AT&T would be precluded from offering the services described in the FCC's *Computer II* decision. In that decision, the FCC ruled that AT&T could offer so-called "enhanced services" (which are essentially the equivalent of the "information services" described in the proposed decree), and customer premises equipment on a nontariffed competitive basis, provided that AT&T does so through a fully separate subsidiary. The Commission's decision simply means that AT&T is authorized, as opposed to required, to offer these services *under the Communications Act;* it does not relieve AT&T of its obligations under the *antitrust laws*, and more specifically under the 1956 decree. (The Commission's decision is presently on review — see *Computer & Communications Industry Ass'n* v. *FCC*, D.C. Civ. No. 80-1471 (filed May 15, 1981) — but the appeal does not alter the underlying legal effect of the Commission's decision in relation to the action before this Court.)

Finally, it should be noted that, if presented with the issue of whether AT&T is precluded by the 1956 decree from offering these non-tariffed competitive services permitted under *Computer II*, this Court would be deciding that issue *de novo*, because the opinion and order issued by Judge Biunno construing the decree to permit AT&T to offer these services has been vacated by order of the Court of Appeals for the Third Circuit. See *United States* v. *Western Electric Co.*, No. 81-1960 (3rd Cir. Feb. 2, 1982); *United States* v. *Western Electric Co.*, No. 49-17 (D.N.J. March 12, 1982).

development would be in the public interest.[199] It will accordingly be approved. By contrast, others who have submitted comments object to AT&T's entry into the information services market.

"Information services" are defined in the proposed decree at Section IV(J) as:

> the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing or making available information which may be conveyed via telecommunications. . . .

Two distinctly different types of information services fall within this general category: services which would involve no control by AT&T over the content of the information other than for transmission purposes (such as the traditional data processing services), and services in which AT&T would control both the transmission of the information and its content (such as news or entertainment). Because these two types of services raise different concerns, they will be addressed separately.

### A. Data Processing and Other Computer-Related Services

As technology has advanced, the line between communications and data processing has become blurred. Advances

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[199] Without control of the local exchange monopolies, AT&T will have no improper advantage over other competitors. See Part IV(B) *supra*. It will not be able to subsidize its offerings with monopoly profits in the interexchange or telecommunications equipment markets (see Part V, *supra*) and there is little likelihood of customer discrimination because these products and services, unlike information services, are not closely dependent upon access to the telecommunications network.

If a potential competitor poses no threat to the development of a healthy competitive market it should obviously not be barred from entering that market. The greater the number of competitors, the more likely it is that consumers will reap the benefits of lower prices and product improvements. AT&T is likely to be an especially potent competitor given its manufacturing expertise and the resources of Bell Laboratories.

in communications technology, for example, now allow otherwise incompatible computers to converse with each other. New sophisticated telephone equipment located on a customer's premises not only performs switching and call routing functions but it also retrieves information much as does a traditional computer. Even ordinary telephones may be capable of performing functions that formerly required the support of a separate computer.[200]

Providers of data processing services — like others who have commented on the decree in other contexts — contend that AT&T should be prohibited from entering these fields because of its market power in the area of interexchange services. Shaping the argument to support their particular interests, these persons contend that AT&T will use the monopoly profits from its interexchange services to subsidize its computer-related services, and that it will use its control over the interexchange network to discriminate against other data processing competitors in providing access to that network.

As explained in Part V *supra*, there is little possibility that AT&T will be able to use its revenues from the interexchange market to subsidize its prices for computer services. That being true, AT&T would not possess any anticompetitive advantages over competitors on this basis, and the possibility of cross subsidization as a basis for rejecting this portion of the proposed decree may therefore be completely discounted.

The discrimination argument is slightly more serious. Since AT&T will be offering its own computer-related services, it may well have an incentive to discriminate in transmitting competitors' services. But what defeats the objections is that AT&T's actual ability to discriminate is quite remote. This segment of the information services industry is already well

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[200] Other examples of these services include AT&T's Custom Calling II (which allows advance calling and call answering), telephone-operated burglar alarm systems, and office management systems (which may provide such diverse functions as inventory control, temperature control, and interoffice data communications).

established, comprised of some of the nation's leading corporate giants, as well as many smaller concerns. The FCC has found that "[t]here are literally thousands of unregulated computer service vendors offering competing services connected to the interstate telecommunications network." *Computer II*, *supra*, 77 F.C.C.2d at 426. These strongly competitive conditions will limit AT&T's ability to practice discrimination in two ways. First, AT&T's competitors will have the economic resources necessary to combat any attempt at discrimination. Second, the growing demand for information services will necessarily increase the demand for transmission facilities for these services. Such an increase in demand is likely to stimulate AT&T's interexchange competitors to offer satisfactory alternatives to the AT&T network,[201] and any attempt by AT&T to discriminate would only further enhance this eventuality.

This fairly limited possibility of discrimination clearly does not outweigh the substantial advantages to the public that would be gained by allowing AT&T to develop this new technology. AT&T's entry into these technologically sophisticated fields will stimulate competition, and it is therefore likely to produce further technological advances, new products, and better services—all of which are likely to benefit the American consumer, American foreign trade, and national defense.

Since AT&T's participation in these areas will foster the traditional objectives of the Sherman Act and is not likely to lead to anticompetitive practices,[202] the Court will not sustain the objections to this aspect of the proposed decree.[203]

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[201] Indeed, some of the providers of these information services may themselves have the resources to construct such transmission systems.

[202] Absent the divestiture of the Operating Companies, that conclusion might, of course, be quite different.

[203] For the reasons stated in Part VII *supra*, the Court also rejects the suggestion that AT&T be required to offer these services through a separate subsidiary.

B. Electronic Publishing Services[204]

The second type of information service which AT&T would be permitted to provide under the proposed decree are those services in which it would control, or have a financial interest in, the content of the information being transmitted. Those services are generally referred to as electronic publishing or information publishing services.[205]

A number of organizations have objected to entry of the proposed decree unless it is modified to include a ban on electronic publishing. However, the decree itself does not specifically refer to the concept of electronic publishing, let alone provide a suitable definition. In order to conduct a meaningful discussion of the relevant issues, therefore, electronic publishing must first be defined. After drawing on various sources,[206] the Court has concluded that, for purposes of this opinion, electronic publishing[207] will be regarded as:

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[204] The discussion of electronic publishing under the topic heading "1956 Consent Decree and Line of Business Restrictions" is for the sake of convenience only. The Court's decision — that permitting AT&T to become an electronic publisher is not in the public interest — was made solely on the basis of the proposed decree here under review and without consideration of whether AT&T could offer these services under the terms of the 1956 decree. But see note 198 *supra*.

[205] For purposes of this discussion, the Court will use the term electronic publishing. Use of this term is not meant to imply a limitation to a particular kind of transmission technology.

[206] The kinds of services here under review have been discussed under a variety of labels in a number of forums. The telecommunications bill introduced in the House of Representatives, for example, used the term "information publishing service" which was defined as:

> provision to any unaffiliated person of any information —
>
> (A) which the publisher has (or has caused to be) authored, originated, gathered, collected, produced, compiled, edited, categorized, or indexed; or
>
> (B) in which the publisher has a direct or indirect financial or proprietary interest.

H.R. 5158, 97th Cong., 1st Sess. § 263(f)(3) (1982). (The bill was withdrawn by Congressman Wirth on July 20, 1982).

A Senate bill on the same subject referred to "cable service" and "mass media services." The former term was defined as "the retransmission of

the provision of any information which a provider or publisher has, or has caused to be originated, authored, compiled, collected, or edited, or in which he has a direct or indirect financial or proprietary interest, and which is disseminated to an unaffiliated person through some electronic means.[206]

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any television or radio broadcasting signal, or program origination, for distribution by cable or any other closed transmission medium to multiple subscribers who pay to receive such service." Mass media services were defined as follows:

> The term 'mass media' includes television and radio broadcasting, pay television, and printed or electronic publications (including newspapers, periodicals, and any service or product like or similar to a newspaper or periodical). Such term does not include —
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> (A) telephone number or address listings and directory assistance (limited to telephone number, address, and business category);
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> (B) weather, time, or sports information;
>
> (C) any information service which AT&T or any affiliate was engaged in on April 7, 1981; or
>
> (D) printed or electronic directory advertising.

S. 898, 97th Cong., 1st Sess. § 229(f) (1981).

Some persons who have commented in this proceeding have urged the Court to adopt the definition used in H.R. 5158; others have proposed their own definition. The National Association of Broadcasters, et al. (Topic 6 Brief at 2), for example, urges that electronic publishing be defined as

> the provision of any information which the provider (the publisher), has, or has caused to be, originated, created, compiled, produced or selected, and which is intended for members of the public and is distributed via electronic means.

[207] In addition to the one-way dissemination of information that is the norm in print publishing, electronic publishing also includes interactive transaction services. These services allow a consumer not only to receive information at home but also to send information back to the publisher. Thus, consumers using a "shop-at-home" service, for example, could use their home terminals to call up information on products being offered by a particular merchant, and then place their orders for the desired products by using their terminals to key in the necessary ordering information.

[208] The kinds of information referred to in this definition include news, business and financial reports, editorials, columns, sports, features, and electronic advertising. The means of transmission include pay television, radio and television broadcasting, and electronic publications which appear either by audio means, on video screens, or in printed form. But see note 223 *infra*. See also S. Rep. No. 97-170, 97th Cong., 1st Sess. 42-44 (1981).

A number of persons have argued that because of potential dangers to competition and to First Amendment values, AT&T should be prohibited from engaging in such activities. For the reasons stated below, the Court agrees.

The threat to competition that is claimed to be posed by AT&T in this industry is that, through the use of cross-subsidization and customer discrimination, it will use its power in the interexchange market to disadvantage competing electronic publishers.[209] While the possibility of cross-subsidization is as remote here as it is with respect to other subjects considered herein,[210] there is a real danger that AT&T will use its control of the interexchange network to undermine competing publishing ventures.

AT&T could discriminate against competing electronic publishers in a variety of ways. It could, for example, use its control over the network to give priority to traffic from its own publishing operations over that of competitors. A second concern is that, inasmuch as AT&T has access to signalling and traffic data, it might gain proprietary information about its competitors' publishing services. Furthermore, it appears that AT&T would have both the incentive and the opportunity to develop technology, facilities, and services that favor its own publishing operations and the areas served by these operations rather than the operations of the publishing industry at large. Similarly, AT&T could discriminate in interconnecting competitors to the network and in providing needed maintenance on competitors' lines. Finally, AT&T might submit tariffs that would have the effect of favoring AT&T's publishing operations to the disadvantage of competing concerns.

AT&T and the Department of Justice provide the same response to these arguments that they make in other contexts: that market forces will curtail AT&T's ability effectively to engage in these practices. In the absence of special problems

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[209] These are the same problems that have been claimed to exist in other markets, but as is apparent from discussion below, they take on a different and more serious complexion in this context.

[210] See Parts V(A) and VI(A) *supra*.

and concerns relating only to the electronic publishing industry, the Court probably would, as it has in other instances, accept that response. However, in the view of the Court a different conclusion is appropriate here, for the peculiar characteristics of the electronic publishing market would both render anticompetitive acts more damaging to AT&T's competitors in that market and insulate such acts from correction by market forces.

The electronic publishing industry is still in its infancy. Although this business may some day be a very significant part of the American communications system, at present, and most likely for the next several years, a small number of relatively small firms will be experimenting with new technology to provide services to an American public that is, for the most part, still almost totally unfamiliar with them. There can be no doubt that, if AT&T entered this market, the combination of its financial, technological, manufacturing, and marketing resources would dwarf any efforts of its competitors.[21] In fact, AT&T's mere presence in the electronic publishing area would be likely to deter other potential competitors from even entering the market.

It is also readily apparent that competitors in the electronic publishing industry — far more so than competitors in any other industry — could easily be crushed were AT&T to engage in the types of anticompetitive behavior described above. Unlike most products and services, information in general and news in particular are by definition especially sensitive to even small impediments or delays. Information is only valuable if it is timely; by and large it is virtually worthless if its dissemination is delayed. This quality is especially important in electronic publishing because up-to-date information and constant availability are the features likely to be sought by subscribers.

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[21] AT&T has already played a major role in developing technical standards for that industry as evidenced by its involvement in writing the "Presentation Level Protocol" which will be used to code electronic publishing signals and which may become the major protocol used by publishers in the United States.

The trial record in the *AT&T* case reveals many instances when AT&T was slow to respond to the needs of competitors, both in providing essential products or parts and in servicing these products and parts.[212] Any delays of that kind, were they to occur in the context of the transmission of electronic publishing information, would quickly cause subscribers to desert their unreliable publishers and thus cripple AT&T's competitors in that business.

Finally, electronic publishers remain more dependent upon the AT&T network than others in the telecommunications business. In some areas, AT&T is the sole provider of intercity services. Elsewhere, where competition does exist, the other common carriers — although capable of handling voice transmissions — frequently lack the sophisticated facilities necessary to meet the needs of the electronic publishers.[213] Systems that are specifically designed to transmit data do not provide a satisfactory solution; most of these systems lease part, if not all, their facilities from AT&T. Nor are satellites the answer, for at least for the present they do not appear to present a realistic alternative, given their restricted availability, potential transmission problems, and high costs.

Thus, should AT&T engage in anticompetitive activity, publishers would have no realistic alternative transmission

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[212] See, *e.g.*, Testimony of Lowell Hoxie (March 10, 1981); Pier Abetti (March 11, 1981); and Luther R. Hinton (March 20, 1981).

[213] For example, the networks of the other common carriers may not be extensive enough to connect a publisher, or a publisher's customers, to the required data bases without relying at least in part on facilities provided by AT&T. Moreover, because competing facilities are not as extensive as AT&T's, the likelihood of congestion on their transmission lines, which causes the calls to receive busy signals, is far greater.

It is of course possible that these publishers could use any alternate transmission systems developed to service the needs of providers of other types of information services. However, it is not clear that those networks will develop in ways which will meet the needs of electronic publishers. Therefore, they cannot be relied upon to serve as a check upon AT&T's power.

system by which to reach their subscribers. The low level of demand for these services that exists at present makes it unlikely that competing interexchange carriers would construct transmission systems to be used solely for the delivery of electronic publishing services, and publishers would therefore be forced to accept the inferior services provided by AT&T.

Based on competitive considerations alone, therefore, the Court might well be justified in barring AT&T from electronic publishing industry. Beyond that, AT&T's entry into the electronic publishing market also poses a substantial danger to First Amendment values.

The goal of the First Amendment is to achieve "the widest possible dissemination of information from diverse and antagonistic sources." *Associated Press* v. *United States*, 326 U.S. 1, 20 (1945). See also *FCC* v. *National Citizens Committee for Broadcasting*, 436 U.S. 775, 795 (1978). This interest in diversity has been recognized time and again by various courts. In *Red Lion Broadcasting* v. *FCC*, 395 U.S. 367, 390 (1969), for example, the Supreme Court observed that

> [i]t is the purpose of the First Amendment to preserve an uninhibited marketplace of ideas in which truth will ultimately prevail, rather than to countenance monopolization of that market.

See also *New York Times Co.* v. *Sullivan*, 376 U.S. 254, 270 (1964). Judge Learned Hand, speaking for the Court of Appeals for the Second Circuit, similarly noted that the media serve "one of the most vital of all general interests: the dissemination of news from as many different sources, and with as many different facets and colors as possible."[214] *United*

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[214] The court further explained that this diversity is essential because the First Amendment "presupposes that right conclusions are more likely to be gathered out of a multitude of tongues, than through any kind of authoritative selection. To many this is, and always will be, folly; but we staked upon it our all." *Id.*

*States* v. *Associated Press*, 52 F. Supp. 362, 372 (S.D.N.Y. 1943), *aff'd*, 321 U.S. 1 (1945).[215]

The striving for diversity in sources of information has found expression not merely in the traditional and constitutional prohibition on control of news by government but also in some private contexts, notably in regard to the broadcast media. The Federal Communications Commission is charged by the Communications Act with granting broadcast licenses in the "public interest, convenience and necessity." 47 U.S.C. §§ 301, 303, 307, 309. Pursuant to that public interest standard, the Commission has time and again adopted rules designed to promote diversity among the broadcast media.[216] These rules, and the policies underlying them have repeatedly been sustained by the Supreme Court and the Court of Appeals for this Circuit.

For example, in *United States* v. *Storer Broadcasting Co.*, 351 U.S. 192, 201-04 (1956), the Supreme Court recognizing the importance of diversity and the authority of the FCC to determine the public interest, upheld rules placing limitations on the total number of broadcast stations a person may own or control. See also, *National Broadcasting Co.* v. *United States*, 319 U.S. 1980 (1943). Likewise, in *FCC* v. *National Citizens Committee for Broadcasting*, 436 U.S. 775 (1978),

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[215] Both the chairman of the House Subcommittee on Telecommunications, Consumer Protection, and Finance and AT&T agree with this principle. Congressman Timothy E. Wirth has aptly pointed out that "the information market provides much more than economic good, for assuring a diversity of information sources is critical to the proper functioning of the entire democratic system." Hearings on H.R. 5158, *supra*, note 141 at Part 3, p. 1. Similarly, Charles Marshall, an AT&T executive vice president, recently testified before the same subcommittee that "the best way to assure a diversity of these kinds of information services to the American public is to assure a diversity of sources." Hearings on H.R. 5158, *supra*, note 141, at Part 2, p. 137.

[216] FCC policies prohibit formation or transfer of co-located newspaper-broadcast combinations (*FCC* v. *National Citizens Committee*, *supra*, 436 U.S. 775 (1978)); common ownership of more than one broadcast station in the same area (47 C.F.R. § 73.35, 73.240, 73.636); operation of cable systems by a telephone company (47 C.F.R. § 63.54); and ownership of cable systems by a television network (47 C.F.R. § 74.1131).

the Court sustained regulations which banned the award or transfer of a broadcast license where there was a common ownership of a broadcast station and a daily newspaper located in the same locality, stating (436 U.S. at 801-02),

> . . . the Commission has acted 'to enhance the diversity of information heard by the public . . . .' The regulations are a reasonable means of promoting the public interest in diversified mass communications.[217]

Certainly, the Court does not here sit to decide on the allocation of broadcast licenses. Yet, like the FCC, it is called upon to make a judgment with respect to the public interest and, like the FCC, it must make that decision with respect to a regulated industry and a regulated company.

In determining whether the proposed decree is in the public interest, the Court must take into account the decree's effects on other public policies, such as the First Amendment principle of diversity in dissemination of information to the American public. See part II *supra*. Consideration of this policy is especially appropriate because, as the Supreme Court has recognized, in promoting diversity in sources of information, the values underlying the First Amendment coincide with the policy of the antitrust laws. *FCC* v. *National Citizens Committee for Broadcasting*, *supra*, 436 U.S. at 800, n. 18.

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[217] The Court of Appeals, speaking in the same case, was even more explicit.

> . . . Congress moved under the spur of a widespread fear that in the absence of governmental control the public interest might be subordinated to monopolistic domination in the broadcast field [citing case] . . . . The First Amendment 'rests on the assumption that the widest possible dissemination of information from diverse and antagonistic sources is essential to the welfare of the public. [citing case]. The 'public interest' standard necessarily invites reference to First Amendment principles . . . .' Although no provision of the Communications Act expresely grants the Commission authority to restrict newspaper ownership of broadcast stations, such express authority is not essential to the validity of Commission regulations. 47 U.S.C. § 309(a) requires the Commission to find the 'public interest, convenience and necessity will be served' by the grant of a license.

*National Citizens Committee for Broadcasting* v. *FCC*, 555 F.2d 938, 948-51 (1977), *aff'd in part*, 436 U.S. 190 (1978).

Applying this diversity principle to the issue here under discussion, it is clear that permitting AT&T to become an electronic publisher will not further the public interest.

During the last thirty years, there has been an unremitting trend toward concentration in the ownership and control of the media. Diversity has disappeared in many areas; newspapers have gone out of business; others have merged; and much of the flow of news and editorial opinion appears more and more to be controlled and shaped by the three television networks and a handful of news magazines and metropolitan newspapers.

This concentration presents obvious dangers even today. Unless care is taken, both the concentration and the attendant dangers will be significantly increased by the new technologies. Indeed, it is not at all inconceivable that electronic publishing, with its speed and convenience will eventually overshadow the more traditional news media, and that a single electronic publisher would acquire substantial control over the provision of news in large parts of the United States. See also part IV(A) *supra*.[218]

The concentration that now exists in the media has presumably been brought about by impersonal economic and technological forces, and it is obviously beyond the concern of this or any other court. But the particular concentration

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[218] De Tocqueville observed with his usual prescience long ago that revolutions by means of the press would most likely come about from its centralization in a few powerful organs. A. de Tocqueville, *Democracy in America* (1835) chapter XI. Richard Reeves who recently retraced de Tocqueville's travels, took note of the development of two-way telecommunications which allowed citizens instantaneously to record their thoughts on the political issues of the day, and he commented that

> [w]hoever decides which questions are to be asked and how they are to be worded has enormous power . . . . The results of these instant referenda would then be flashing in front of each legislator. A member of Congress, knowing public opinion in the district or the country, would then have the dubious honor and politically dangerous duty of voting, perhaps testing his or her conscience against the recorded will of the majority.

R. Reeves, *American Journey* 89–90 (1982).

that may emerge from the proposed decree is subject to the Court's jurisdiction in this antitrust case as part of the instant proceeding. Not only is AT&T a regulated company, and not only does the proceeding stem directly from serious charges of anticompetitive conduct, but the Court has been mandated not to approve the proposed decree unless it finds it to be in the public interest. AT&T's ability, described above, to use its control of the interexchange network to reduce or eliminate competition in the electronic publishing industry is the source of this threat to the First Amendment principle of diversity.

In sum, for a variety of reasons, the entry of AT&T into electronic publishing involves risks to the public interest that are greater than those which would be involved by that company's entry into other markets. Since under the Sherman Act, it is appropriate to bar a company from a market if the restriction is necessaray to permit the development of competition in that market (*Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at 577-78),[219] and since First Amendment values, too, support a ban on electronic publishing by AT&T, the Court will require that the company be prohibited from entering the market.[220]

At the same time, a prohibition on electronic publishing does not impose an undue burden on AT&T.[221] The company is free to enter all the other computer, computer-related, and information services markets; and it will simply be barred from the creation or control of the information to be trans-

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[219] The Court explicitly rejected Ford's argument that the manufacturing prohibition removed a potential competitor from the market, finding that the restriction was necessary to allow the development of competition in the industry. *Id.*

[220] Such a prohibition will not have anticompetitive consequences because AT&T has no special expertise in creating information which would make it a potent competitor in this market. It could overwhelm competitors only because of its ability to engage in anticompetitive conduct.

[221] The Court notes that AT&T has stated that, although it does not wish to be legally bound, "it now has no intention to provide information services that would be competitive with the news and features of newspaper or with broadcasting or traditional cable television services." AT&T Reply Brief, p. 115.

mitted.[222] AT&T may thus fulfill its traditional function of providing a delivery system for information which others wish to transmit, and it may also manufacture and market equipment for the electronic publishing industry and provide transmission services for other electronic publishers.[223]

The restriction on electronic publishing — like any limitation on competition — should only remain in effect for the period necessary to establish conditions conducive to free and fair competition. Since it is not likely that the factors enumerated above which militate against AT&T's immediate entry into the electronic publishing market will continue to exist indefinitely, the Court will place a time limit on its prohibition. See *Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at pp. 562, 575 n. 10, where the Court upheld an antitrust decree that prohibited Ford from entering the spark plug manufacturing business but limited that prohibition to a period of ten years.

Section VII of the proposed decree allows modifications to be made in its provisions upon the application of a party or an Operating Company. It is the intention of the Court to remove the prohibition on electronic publishing at the end of seven years from the entry of the decree should application for such removal be made pursuant to Section VII. That

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[222] AT&T may engage in this activity if the information is delivered over transmission facilities in which AT&T has no interest. In that case, there would be no possibility of anticompetitive activity, because AT&T would have no control over the transmission of its publishing services.

[223] Beyond that, the Bell System has long been engaged in providing a variety of services which, although relatively minor in character, could loosely be regarded as falling into the category of electronic publishing. Because of that involvement without significant adverse consequences, it is not necessary in the public interest that AT&T be precluded, and AT&T will not be precluded, by the modification required below, from offering the following: electronic directory services including listings of general product and business categories, and of the service or product providers under these categories, and their names, telephone numbers, and addresses; such traditional Bell System services as time, weather, and such other audio services as are being offered as of the date of the entry of the decree to the geographic areas of the country receiving those services as of that date; and the dissimination of information to and from AT&T's affiliates.

seven-year period should be sufficient for the development of electronic publishing as a viable industry, for the acquisition of sufficient strength by individual publishers adequate to permit them to compete, and for the development of means other than the AT&T network for the transmission of the messages of electronic publishers. During that same period, the new AT&T will also have acquired a track record with respect to behavior toward its competitors in other areas of the telecommunications business.[224]

## VII

### Restrictions on the Divested Operating Companies

The proposed decree limits the Operating Companies, upon their divestiture, to the business of supplying local telephone service. In addition to a general prohibition against the provision of "any product or service that is not a natural monopoly service actually regulated by tariff," there are more specific restrictions in Section II(D) which deny the Operating Companies the opportunity to engage in the following activities: (1) the provision of interexchange services; (2) the provision of information services; (3) the manufacture of telecommunications products and customer premises equipment; (4) the marketing of such equipment and (5) directory advertising, including the production of the "Yellow Pages"[225] directories.[226]

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[224] The Court expects to allow any opponents of the removal of the prohibition to comment on the question whether its continuation will be in the public interest, and, should they be able to show that competitive conditions clearly require the maintenance of the ban, it will not be lifted. However, the burden will at that time be on such opponents to demonstrate that the public interest requires the continued exclusion of AT&T from electronic publishing.

[225] These are the directories currently produced by the Operating Companies or under their auspices, for each geographic region which they serve. These directories contain subscriber listings grouped by subject matter along with advertisements.

[226] No specific provision of the proposed decree deals with directory advertising, but the parties have stated that the general prohibition against provision of non-monopoly services includes production of the Yellow Pages. See Competitive Impact Statement at 29 n. 24.

Restrictions of this type may validly be imposed if they are necessary to prevent the occurrence or recurrence of anticompetitive conduct. *Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at 577-78. See Part II *supra*. However, as the Department of Justice[227] concedes, such restrictions deserve "the most careful scrutiny" to ensure both that they will have the desired effect and that they will not actually limit competition by unnecessarily barring a competitor from a market. Department of Justice Response to Comments at 56.

These restrictions are justified, according to the Department, because the Operating Companies will have "both the ability and the incentive" to thwart competition in these markets by leveraging their monopoly power in the intraexchange telecommunications market.[228] In the absence of the restrictions, it is reasoned, the Operating Companies will be able (1) to subsidize their prices in competitive markets with supracompetitive profits earned in the monopoly market, and (2) to hinder competitors by restricting their access to the intraexchange network. In short, it is the Department's view that the divested Operating Companies may appropriately be equated with the present Bell System complex in that, if permitted to enter competitive markets, they may be expected to engage in the same type of anticompetitive behavior that was the crux of the *AT&T* lawsuit.

The government's approach, while not without conceptual neatness, fails to take account of circumstances far more complex than these undifferentiated rules acknowledge. The Bell System is a vast, vertically integrated company which dominates local telecommunications, intercity telecommunications, telecommunications research, and the production and marketing of equipment. Each of the divested Operating Companies will have a monopoly in only one geographic

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[227] It appears that the Department is the principal proponent of the restrictions on the Operating Companies. AT&T has generally taken the stance that it agreed to these restrictions as part of the overall settlement.

[228] Response to Comments at 54. See also *id.* at 58-61; Competitive Impact Statement at 27.

portion of one of these markets — local telecommunications. In addition, the Bell System as presently constituted has few powerful competitors in any of the activities in which it is engaged. The Operating Companies, by contrast, will, if permitted to enter competitive markets, be faced with the most potent conceivable competitor: AT&T itself. Thus, the only similarity between the divested Operating Companies and the present Bell System is that both possess a monopoly in local telecommunications.

That single circumstance — important though it may be — is not a sufficient basis upon which to restrict competition generally in the name of the antitrust laws. If this were the case, all monopolies might have to be barred from competitive industries, and even the Department of Justice acknowledges that this drastic remedy is not required. See Response to Comments at 55. The Tunney Act's public interest standard permits the Operating Companies to be barred from a competitive market only if there is a substantial possibility that they will use monopoly power to impede competition in that market. Two basic factors are relevant to this determination.

The restrictions are based upon the assumption that the Operating Companies, were they allowed to enter the forbidden markets, would use their monopoly power in an anticompetitive manner. It is accordingly necessary for the Court first to determine whether these companies will actually have the incentive and opportunity to act anticompetitively.[229] Second, the restrictions are, at least in one sense, directly anticompetitive because they prevent a potential competitor from entering the market. The Court must accordingly also consider the extent to which the participation of the Operating Companies would contribute to the creation of a competitive market.[230]

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[229] The Court cannot accept the proposition advanced by some that state and federal regulation alone will eliminate the possibility of anticompetitive abuses by the Operataing Companies. If regulation could effectively prevent these practices, there would have been no need for the *AT&T* action. See part IV *supra*.

[230] There is no basis for the government's contention that the participation of the Operating Companies in these markets would be of little competitive

In addition, the Court must assess the effect of the restrictions upon other important public policies. Many persons,[231] including particularly the States, claim that these restrictions would have adverse consequences in that they would either undermine the financial viability of the divested Operating Companies, or produce substantial increases in the rates for local telephone service, thus eroding the statutory goal of universal telephone service for all Americans. See 47 U.S.C. § 151.[232] This factor, to be sure, cannot preclude the imposition of a restriction necessary to preclude the anticompetitive activity; but to the extent that a restriction does not have a procompetitive effect, it may not be imposed if it infringes upon other public policies. See generally Part II *supra*.

The Court will examine the various substantive provisions in light of these general principles.[233]

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value. Their expertise in telecommunications and their large customer base would make them natural competitors in these fields.

[231] Including the members of the House Subcommittee on Telecommunications, Consumer Protection, and Finance who submitted their views to the Court. See note 63 *supra*.

[232] Evidence introduced during the *AT&T* trial indicated a definite correlation between increases in local telephone rates and the number of homes with a telephone. See Testimony of Louis J. Perl (November 23, 1981); Exhibit D-4-1518.

[233] Some have contended that the Court should not assess the propriety of the restrictions without holding evidentiary hearings with regard to the need therefor, their effect upon local rates, and related matters. The legislative history of the Tunney Act indicates that the court reviewing a proposed consent decree has broad discretion in fashioning the procedures for the public interest review. Both congressional committees stated, "Only where it is imperative that the court should resort to calling witnesses for the purpose of eliciting additional facts should it do so." S. Rep. No. 93-298, *supra*, at 6-7; H.R. Rep. No. 93-1463, *supra*, at 8. The record in the *AT&T* action contains extensive information about the competitive structure of the entire telecommunications industry. This Court has relied upon that record in assessing the competitive significance of the proposed restrictions, and an evidentiary hearing concerning such matters is therefore not necessary.

Similarly, there is no need for a hearing concerning the effect of the restrictions upon local rates. Any testimony on that issue could only be speculative and would be unlikely to assist the Court in its public interest

A. Interexchange Services

The proposed decree prohibits the divested Operating Companies from providing interexchange services. This restriction is clearly necessary to preserve free competition in the interexchange market.

Access to the local exchange is essential for all interexchange carriers and, as the evidence in the *AT&T* action has suggested, there are many ways in which the company controlling the local exchange monopoly could discriminate against competitors in the interexchange market. See Part IV *supra*. After divestiture, the Operating Companies' incentives to engage in such activity will remain unchanged: they would stand to gain business if other carriers were disadvantaged by poor access arrangements and high tariffs.

To permit the Operating Companies to compete in this market would be to undermine the very purpose of the proposed decree — to create a truly competitive environment in the telecommunications industry. The key to interexchange competition is the full implementation of the decree's equal exchange access provisions. See Part VIII *infra*. If the Operating Companies were free to provide interexchange service in competition with the other carriers, they would have substantial incentives to subvert these equal access requirements. The complexity of the telcommunications network would make it possible for them to establish and maintain an access plan that would provide to their own interexchange service more favorable treatment than that granted to the other carriers. Such a result would perpetuate the very inequalities that the proposed decree is designed to eliminate. Finally, the Operating Companies would also retain the ability to subsidize their interexchange prices with profits earned from their monopoly services.

Those who object to this restriction suggest (1) that the Operating Companies would provide additional competition in the interexchange market and (2) that revenues from

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determination. In addition, the effect of the restrictions upon local rates does not represent the crux of the Court's decision on these quesitons.

interexchange operations would increase that viability and reduce the need for local rate increases. These objections have little merit in this context. If the Operating Companies entered the interexchange market and competed fairly, without exploiting their local monopoly positions, the resulting increase in competition would not be substantial.[234] Moreover, the Operating Companies could realistically recoup substantial profits from their interexchange operations only by using their monopoly power to disadvantage competitors.[235] But that, of course, would be precisely the behavior which brought about the 1974 lawsuit against AT&T and the current proposal for a decree. In short, there are clear, and indeed overwhelming, procompetitive justifications for this restriction.[236]

B. Information Services

The proposed decree prohibits the Operating Companies from providing information services, an umbrella description of a variety of services including electronic publishing and other enhanced uses of telecommunications.[237] This prohibition is necessary for reasons similar to those justifying the restriction on interexchange services, as well as for additional reasons not relevant to the interexchange problem.

All information services are provided directly via the telecommunications network. The Operating Companies would therefore have the same incentives and the same ability to

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[234] The Operating Companies would simply be additional competitors in a market that is already quite competitive. See Part V *supra*.

[235] Competition in the interexchange market would tend to drive prices close to costs. Thus, absent anticompetitive activity, it is unlikely that the Operating Companies would be able to earn a profit large enough to provide any meaningful subsidy to local rates.

[236] The proposed decree's clauses permitting AT&T to provide some intraexchange services in competition with the Operating Companies are not inconsistent with this result. AT&T will not have the power to disadvantage the Operating Companies because the local companies do not require access to AT&T's network to provide exchange telecommunications. It is AT&T that will be dependent upon the Operating Companies for access to its customers, not vice versa.

[237] For a full discussion of the meaning of this term see Part VI *supra*.

discriminate against competing information service providers that they have with respect to competing interexchange carriers. Here, too, the Operating Companies could discriminate by providing more favorable access to the local network for their own information services than to the information services provided by competitors, and here, too, they would be able to subsidize the prices of their services with revenues from the local exchange monopoly.[238]

There is also the effect on the configuration of the local networks to consider. Many of the competitive problems in the interexchange market resulted from the fact that competition was introduced after AT&T had designed the local networks to service only its own Long Lines department. If the Operating Companies are excluded from the information services market, they will have an incentive, as time goes on, to design their local networks to accommodate the maximum number of information service providers, since the greater the number of carriers the greater will be the Operating Companies' earnings from access fees. Thus, competition will be encouraged from the outset. If, however, the Operating Companies were permitted to provide their own information services, their incentive would be the precise opposite: it would be to design their local networks to discourage competitors, and thus to thwart the development of a healthy, competitive market.[239]

The restriction on the provision of information services by the Operating Companies has been attacked on the ground

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[238] For similar reasons, the Court rejects the argument that the Operating Companies can most efficiently provide information services by taking advantage of various economies (such as using the same equipment for exchange telecommunications and for information services). It would be impossible to determine at any time whether the Operating Companies' advantages were due to inherent efficiencies, or to efficiencies created by structuring the network so as to hinder competition. The experience with AT&T's activities with regard to interexchange competition indicates that the latter is a possibility which would be difficult to detect or prevent.

[239] The reasons underlying the ban on provision of electronic publishing services by AT&T provide further support for restricting the Operating Companies from this activity. See Part VI *supra*.

that it will remove their incentive to upgrade the local networks and will cause them to become technological backwaters.[240] This claim underrates the role of the Operating Companies under the proposed decree. These companies will carry traffic between the information service providers and their subscribers; their networks will therefore have to be capable of carrying these technologically advanced services; and they will have a financial incentive to create this capability because they will earn access charges for providing this service.[241]

For all of these reasons, the imposition of this restriction is fully consistent with the antitrust laws.

C. Manufacture of Equipment

The provision in the proposed decree which prohibits the Operating Companies from manufacturing telecommunications equipment and customer premises equipment (CPE)[242] is also an outgrowth of the government's case in the *AT&T* action. The basic rationale of the procurement portion of that case was that

> a combination of vertical integration and rate-of-return regulation . . . tended to generate decisions by the Operating Companies to purchase equipment produced by Western [Electric] that is more expensive or of less quality than that manufactured by the general trade.

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[240] It cannot be claimed that this restriction will result in rate increases: the Operating Companies do not now provide such services on any large scale, and it is not at all clear that they would be a great source of profit to them in the future.

[241] Entry of the Operating Companies into this market is not necessary to provide competition for AT&T. The large amount of interest generated by this growing industry indicates that there will be a number of competitors. See part V(A) *supra*.

[242] Telecommunications equipment is used by a carrier to provide telecommunications services. Proposed Decree, Section IV(N). Customer premises equipment is used on subscriber's premises to originate, route, or terminate telecommunications (*e.g.*, telephone sets, answering machines). Section IV(E).

*United States* v. *AT&T*, *supra*, 524 F. Supp. at 1373. The government presented evidence to support this theory, which tended to show that AT&T headquarters and the service components of the Bell System — the Bell Operating Companies and the Long Lines Department — engaged in systematic efforts to disadvantage outside suppliers. *Id.* at 1371-74. See also Part IV *supra*. That theory and that evidence directly support the proposed prohibition on the manufacture of equipment by the Operating Companies.

There is a substantial likelihood that, should the Operating Companies be permitted to manufacture telecommunications equipment, nonaffiliated manufacturers would be disadvantaged in the sale of such equipment and the development of a competitive market would be frustrated. The Operating Companies would have an incentive to subsidize the prices of their equipment with the revenues from their monopoly services as well as to purchase their own equipment, even though it was more expensive and not of the highest quality. In that respect, the Operating Companies lack the competitive restraints that ordinarily prevent the typical vertically-integrated company from engaging in such practices: the absence of competition in the end product market — exchange telecommunications — immunizes these purchasing decisions from competitive pressures. The Operating Companies therefore would be able to pay inflated prices for poor quality equipment and to reflect these costs in their rates without suffering a diminution in revenues. See *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1373.[243]

Moreover, if they were permitted to manufacture CPE, the Operating Companies would have substantial incentives

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[243] This rationale does not require the divestiture of Western Electric from the Bell System because AT&T's end products — interexchange services and information services — will be subject to competitive pressures. If AT&T paid a higher price for its equipment and that cost was reflected in higher rates, consumers would switch to a carrier with prices which reflected purchasing decisions based upon the principles of best quality and least cost.

to favor their own manufacturing arms by providing to them information regarding changes in network standards, thus permitting them to gain an advantage over non-affiliated manufacturers.[244] In addition, they could subsidize the price of this equipment with revenues from the exchange monopoly.

The risks of anticompetitive behavior are not quite as severe as those which exist in connection with the provision of interexchange and information services. However, they are sufficient to support the imposition of the restriction, especially because the entry of the Operating Companies into this market would not provide any substantial impetus to competition to make any significant contribution to the reduction of local rates. The CPE manufacturing industry already contains numerous competitors, including large domestic and foreign firms, and it is wholly unlikely that the Operating Companies could earn supracompetitive profits in this market that would enable them to subsidize local telephone service. The minimal additional competition which they could provide does not outweigh the substantial possibility that they will engage in anticompetitive conduct.

D. Marketing of Customer Premises Equipment

The proposed decree would also prohibit the Operating Companies from selling or leasing customer premises equipment.[245] While the Department of Justice's comments and

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[244] The Department of Justice acknowledges that the registration program established by the FCC, see 47 C.F.R. §§ 68.1 *et seq.* (1981), would somewhat limit the Operating Companies' opportunities to obstruct the attachment to their networks of equipment manufactured by others. Response to Comments at 67-68. However, it seems possible that, where the Operating Company is the manufacturer of a type of equipment, it would still be able to impose interconnection requirements designed to favor that equipment. In addition, the Operating Companies retain the ability to discriminate against equipment manufactured by others with respect to types of interconnections, testing, maintenance and similar matters.

[245] The proposed decree further prohibits the selling or leasing of telecommunications equipment. However, few objections have been raised against this prohibition. There would appear to be little incentive for the

briefs tend to blur the distinction between manufacturing and marketing, in fact the restrictions on the two activities present wholly different considerations. Based upon a realistic assessment, marketing of CPE presents little potential for anticompetitive behavior by the Operating Companies. While the Operating Companies would have the theoretical ability to engage in the types of anticompetitive activities which support the prohibition on manufacturing of CPE, their incentives and their practical ability to do so would be minimal.

Anticompetitive activities undertaken by two separate corporations rather than by two components of the same corporation are likely to be far more difficult to accomplish because of increased problems of coordination and the greater possibility of detection. For example, it would be quite difficult for an Operating Company to conspire successfully with a manufacturer to provide advance information about revised network standards or to impose interconnection restrictions which favored that manufacturer's products and no one else's.[246]

The possibility of successful subsidization of CPE prices with local exchange revenues appears remote for several reasons. First, since the two businesses are so completely different, the Operating Companies would have little ability to engage in cross subsidization by the sharing of common costs. Second, the participation of a second company would

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Operating Companies to act as retailer for this equipment, since the only purchasers would be telecommunications carriers. In the absence of any reasons for removing the restriction, the need to guard against coordination between manufacturers and the Operating Companies is sufficient justification for this prohibition.

[246] Such interconnection restrictions would be unlikely in any event. See note 244 *supra*. It would be even more difficult, if not impossible, to draft an interconnection standard that favored a piece of equipment sold by an Operating Company but did not likewise favor the same equipment when sold by a competiting retailer. Even if an Operating Company were the exclusive retailer of certain equipment, it probably could not realistically so tailor the standards as to favor the manufacturer of that particular equipment and, should it attempt to do so, the anticompetitive nature of the standard would be apparent on its face.

probably make cross subsidization far easier to detect.[247] Third, the second company's participation in most of the schemes would most likely reduce the profits which the Operating Companies could reap. When these increased risks of detection are combined with the decreased financial gain, it is clear that the incentives for participation of the Operating Companies in cross subsidization schemes are substantially reduced.

As against these relatively slight risks to competition from Operating Company involvement in the marketing of CPE must be weighed the very substantial contribution these companies could make to vigorous competition in the customer premises equipment market. Under the proposed decree, AT&T will retain both the embedded customer premises equipment and the existing network of retail outlets.[248] These factors, combined with Western Electric's large market share,

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[247] The rules governing CPE pricing imposed by the FCC's *Computer II* decision will also make it more difficult to engage in cross subsidization.

[248] There is no reason to change the allocation of these assets provided for in the proposed decree. The embedded CPE consists primarily of Western Electric equipment, and it is therefore appropriately allocated to AT&T. As for the retail stores, there is no basis for concluding that the retention of these assets by AT&T will be anticompetitive. The Operating Companies will have substantial retail access through their contact with the individual telephone subscribers, and they should be able to build their own retail outlets on this basis alone to compete with those of AT&T and others.

Some parties have suggested that the embedded CPE should not be transferred to AT&T, claiming that such a transfer would have a substantial impact upon the Operating Companies' revenues from interexchange activities. This argument apparently proceeds on the theory that the transfer will reduce the Operating Companies' rate bases and therefore also reduce the amount they are entitled to receive under the so-called separations and settlements process for the use of their equipment by interstate traffic. However, the proposed decree eliminates the division of revenues process and mandates its replacement by a system of access charges. Regulatory authorities may set the access charges so as to guarantee the Operating Companies the same amount that they received under the separations process irrespective of the rate base. In addition, the FCC's decision in *Computer II* will, if ultimately upheld on appeal, result in the eventual deregulation of all CPE and its removal from Operating Companies' rate bases in any event.

will at a minimum, ensure its continuation as a formidable provider of CPE for a considerable period of time. The Operating Companies, with their existing relationship to telephone users, are more likely than any other competitive entity to provide an effective counterbalance to AT&T's market strength and thereby to promote a genuinely competitive market.[249]

The Court concludes that, for the reasons stated,[250] the prohibition on marketing by the Operating Companies of customer premises equipment is not in the public interest, and it will therefore require that the proposed decree be modified to eliminate this prohbition.[251]

E. Directory Advertising

Each Bell Operating Company presently publishes Yellow Pages directories for its service area.[252] The proposed decree

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[249] The Operating Companies may be expected to serve as outlets for many of the small equipment manufacturers, providing a stimulus both for price competition and for innovative design and manufacturing. The competitive nature of this market makes it unlikely that the restriction will have an effect upon local rates.

[250] Additionally, as is also true with respect to the probhibition on the production of the Yellow Pages directories (see Subpart E *infra*), the avoidance of an unnecessary intrusion into matters of direct interest to the states and state regulators, supports removal of the prohibition.

[251] A number of persons have urged that, in the event that it is determined that particular restrictions are not in the public interest, the Operating Companies be required to conduct competitive activities through a separate subsidiary. A separate subsidairy does not eliminate economic incentives for anticompetitive conduct; it is simply a method of revealing intracompany transactions so that regulators may more effectively prevent cross subsidization and other improper behavior. See *NARUC* v. *FCC*, 525 F.2d 630, 637 (D.C. Cir. 1976); *Second Computer Inquiry*, *supra* note 17, 77 F.C.C. 2d 384, 462 (1980). In any event, since separate subsidiaries are essentially a regulatory device, it does not seem appropriate, except in the most unusual circumstances, for an antitrust court to impose such a requirement. If the legislators or the regulators should conclude, for their own reasons, that a separate subsidairy would be appropriate, they may, of course, impose this requirement in the exercise of their own responsibilities.

[252] In some cases the directory is published by an independent organization under contract with the Operating Company.

would bar the divested Operating Companies from all activities related to directory advertising, including the production of the so-called Yellow Pages.[253] This restriction lacks an appropriate basis and is not in the public interest.

Neither of the reasons underlying the other restrictions on the Operating Companies — the need to prevent cross subsidization and the importance of preventing competitor discrimination — has any relevance to the printed directory market.[254]

All parties concede that the Yellow Pages currently earn supra-competitive profits. See, *e.g.*, the Department of Justice Response to Comments at 71. There is no warrant therefore for proceeding on the premise that the advertising prices charged by the Operating Companies are artificially low as the result of a subsidy from local exchange service. Similarly, there is no possibility of improper discrimination by the Operating Companies against competing directory manufacturers since access to the local exchange network is not required for production of a printed directory.[255] In short, the Operating Companies would have little or no ability to discriminate against competitors in the printed directory market, and this restriction thus has no procompetitive justification whatever.[256]

To the contrary, the prohibition on directory production by the Operating Companies is distinctly anticompetitive in

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[253] The Operating Companies are appropriately prohibited from producing electronic versions of the Yellow Pages, for the reasons stated in Subpart B *supra*.

[254] The Department of Justice conceded that "we're not so much worried about competition in print." Hearing on June 29, 1982, Tr. 25184.

[255] These competitors only require access to the Operating Companies' subscriber listings, and there is no claim that the Operating Companies have withheld the lists to stifle competition. In fact, under the proposed decree, they would retain control of the listings. Department of Justice Response to Comments at 71.

[256] It does not even seem to be true that, as the Department of Justice assumes, the Yellow Pages fall as a purely formalistic matter on the competitive side of the monopoly-competition dichotomy. See, *e.g.*, Telecommunications Act of 1982 Hearings, *supra* note 141, at Part 1, pp. 551–52.

its effects, for at least two reasons. In the first place, the production of the Yellow Pages will be transferred from a number of smaller entities to one nationwide company — AT&T.[257] This type of concentration is itself anathema to the antitrust laws. Furthermore, possession of the franchise for the printed directories will give AT&T a substantial advantage over its competitors in providing electronic directory advertising[258] — a market in which the Operating Companies will not be engaged.

In addition to these factors directly related to competition, there are other reasons why the prohibition on publication of the Yellow Pages by the Operating Companies is not in the public interest. All those who have commented on or have studied the issue agree that the Yellow Pages provide a significant subsidy to local telephone rates. This subsidy would most likely continue if the Operating Companies were permitted to continue to publish the Yellow Pages.

The loss of this large subsidy would have important consequences for the rates for local telephone service. For example, the State of California claims that a two dollar increase in the rates for monthly telephone service would be

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[257] Although in theory the Yellow Pages would not be directly transferred to AT&T but would merely be made available to the highest bidder, it is clear that AT&T would in reality become the sole publisher of the Yellow Pages in the United States. Under the proposed decree AT&T will retain all of the personnel who have the experience in producing and marketing the Yellow Pages. Moreover, ingrained customer preferences being what they are, it would appear that, if the Operating Companies are not permitted to publish these directories, the only other widely-known telephone company (AT&T itself) will become the natural heir of this enterprise. This is so particularly since that company, with its financial resources, will inevitably be able to outbid anyone else who seriously considered entering this traditional Bell business. The parties do not dispute the conclusion that the business opportunities represented by the Yellow Pages would be transferred to AT&T. AT&T would hardly undertake to guarantee the Operating Companies' net revenue from the Yellow Pages if it did not expect to obtain the contract. See Defendants' Reply Brief at 35.

[258] The large amount of information received by AT&T, combined with the economies of scale, would give it a natural and in all likelihood insuperable edge in the electronic Yellow Pages market.

necessary to offset the loss of revenues from directory advertising.[259] Other states assert that increases of a similar magnitude would be required.[260] Evidence submitted during the *AT&T* trial indicates that large rate increases of this type will reduce the number of households with telephones and increase the disparity, in terms of the availability of telephone service, between low income and well-off citizens.[261] This result is clearly contrary to the goal of providing affordable telephone service for all Americans.[262]

In addition, as noted in Part III(C) *supra*, the Court must take care to intrude upon state regulation only to the extent necessary to vindicate the federal interest embodied in the antitrust laws. Where, as here, that interest is not furthered, intrusion constitutes an impermissible imposition upon the States.

For these various interrelated reasons, the Court accordingly concludes that the prohibition, express or implied, on publication by the Operating Companies of the Yellow Pages directories is not in the public interest. It will therefore require that the proposed judgment be modified to specify that there will be no such prohibition.[263]

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[259] Topic 2 Brief of People of California, *et al.* at 8-9.

[260] Topic 2 Brief of State of Oregon at Appendix A; Topic 2 Brief of State of Florida at 8; Topic 2 Brief of Virginia State Corporation Commission at 12; Topic 2 Brief of Kentucky, *et al.* at Attachment B, p. 2.

[261] See Testimony of Louis C. Perl (November 23, 1981); Exhibit D-4-1518.

[262] Neither AT&T nor the Department of Justice has provided any assurance that this loss of revenue will not occur. AT&T's promise to guarantee the revenues from Yellow Pages for four years is only a short-range solution. The Department of Justice has retreated from its earlier claims that the Operating Companies will receive equivalent revenues under its scheme for the production of Yellow Pages, and it is now apparently unable to predict the level of receipts. Response to Comments at 71–72.

[263] The assets used in the production of these printed directories will accordingly have to be allocated to the Operating Companies. See Part IX *infra*.

F. Removal of the Restrictions

It is probable that, over time, the Operating Companies will lose the ability to leverage their monopoly power into the competitive markets from which they must now be barred. This change could occur as a result of technological developments which eliminate the Operating Companies' local exchange monopoly or from changes in the structures of the competitive markets. In either event, the need for the restrictions upheld in Subparts A through C will disappear, and the decree should therefore contain a mechanism by which they may be removed.[264]

Recognizing this fact, the Department of Justice has undertaken to report to the Court every three years concerning the continuing need for the restrictions imposed by the decree. Response to Comments at 62. In addition, both parties have agreed that the restrictions may be removed over the opposition of a party to the decree when the Court finds that "the rationale for [the restriction] is outmoded by technical developments." Department of Justice Brief at 32–33; AT&T Brief at 18.

The standard for removal of restrictions proposed by the parties incorporates the Department of Justice's view that the restrictions are justified by the mere existence of monopoly power. However, in the opinion of the Court, the removal of the restrictions should be governed by the same standard which the Court has applied in determining whether they are required in the first instance. Thus, a restriction will be removed upon a showing that there is no substantial possibility that an Operating Company could use its monopoly power to impede competition in the relevant market.[265] See pp. 102–103 *supra*. To avoid any question about the appropriate

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[264] If the restrictions were to continue in effect, their sole effect would be to limit competition by preventing the entry of a viable competitor.

[265] This standard necessarily differs from the one governing the termination of the restrictions against AT&T's participation in the electronic publishing industry because different considerations are involved. See Part VI *supra*.

test,[266] the standard for removal of the restrictions should be explicitly incorporated into the decree.[267]

## VIII
## Equal Exchange Access

One of the government's principal contentions in the *AT&T* case was that the Operating Companies provided interconnections to AT&T's intercity competitors which were inferior in many respects to those granted to AT&T's own Long Lines Department. There was ample evidence to sustain these contentions. See Part IV *supra*.

Although after divestiture the Operating Companies will no longer have the same incentive to favor AT&T, a substantial AT&T bias has been designed into the integrated telecommunications network, and the network, of course, remains in that condition. It is imperative that any disparities in interconnection be eliminated so that all interexchange and

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[266] The test usually applied to a contested modification of a consent decree was set forth in *United States* v. *Swift & Co.*, 286 U.S. 106, 118 (1932). In that case, the Supreme Court held that the applicable standard was whether there were "unforseen conditions" that indicated the modification was appropriate. Some parties contend that a different standard may not be applied to the removal of the restrictions. However, there appears to be no reason why the decree itself cannot contain provisions governing the expiration of some of its restrictions.

[267] Some interested persons, including the FCC, contend that the restriction limiting the divested Operating Companies to regulated natural monopoly activities is overbroad because these companies should only be barred from activities in which they may be able improperly to utilize their monopoly power in exchange telecommunications, and that these companies should be free to operate unrelated businesses (*e.g.*, restaurants or department stores). A modification along these lines is not appropriate, if only because it would be extremely difficult to draw a comprehensive definition of the areas in which the Operating Companies' activities must be limited. Moreover, such a definition is unnecessary if the parties include in the proposed decree the Court's standard for the removal of restrictions on the activities of the divested Operating Companies. A divested Operating Company which sought to engage in an unrelated industry could then petition the Court for removal of the restriction as it pertains to that industry, and if there was no realistic possibility of abuse of monopoly power, the Court could simply grant the petition.

information service providers will be able to compete on an equal basis.

The Court has examined the equal access provisions of the decree and it is satisfied that, with limited exceptions, they meet the public interest standard.

A. General Principles

The governing principle established by the proposed decree is that by September 1, 1986, the Operating Companies must provide access services[258] to interexchange carriers and information service providers which are "equal in type, quality, and price" to the access services provided to AT&T and its affiliates. Section II(A). This broad guarantee of equal treatment, when implemented, will effectively remove any interconnection-type obstacles to free competition between AT&T and the other carriers;[259] it therefore comports with the public

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[258] These are the services which permit the origination or termination of an interexchange telephone call and similar transmission assistance for information services.

[259] Several radio common carriers and owners of private communications systems contend that the equal access requirement should also apply to their interconnections with the Operating Companies instead of only to interconnection by the interexchange carriers and information services providers. The Court finds justified the parties' decision not to address these specialized demands.

The access services required by these carriers are likely to differ from those needed by interexchange carriers and to differ also from carrier to carrier. For example, unlike interexchange carriers, owners of private systems are generally satisfied with their present interconnection arrangements (see Comments of Association of American Railroads at 8) but radio carriers wish their services to receive interconnection as would a Bell System Class 5 Switch (see Comments of Telocator Network of America at Appendix E). The decree could not establish all the various standards for interconnection for the large number of systems which seek access to the local networks of the divested Operating Companies. Nor is this necessary, for there is no support for the underlying premise of these carriers' contentions that the divested Operating Companies will have an incentive to alter the existing connecting arrangements for private systems. The question of proper interconnection of radio carriers has been addressed by the FCC and is currently before the Court of Appeals for this Circuit. *Cellular Communications Systems*, 86 F.C.C. 2d 469 (1981), *on reconsid-*

interest and will be endorsed and enforced by the Court.[270]

As indicated, the equal access requirement does not become effective immediately. There is a phase-in period: the Operating Companies must begin offering equal access by 1984; carriers must be able to obtain equal access for one-third of their subscribers by 1985; and such access must be furnished to all subscribers "upon bona fide request" by 1986. The decree also fails to specify the manner in which equal access will be provided; rather, it permits each Operating Company to devise an appropriate plan to fulfill this requirement.[271]

The Court finds these provisions to be reasonable and not inconsistent with public interest. Major changes in switching equipment — such as those that will be necessary to provide equal access to all interexchange and information providers — realistically take months or in some instances years to accomplish.[272] For that reason, the Court could not expect

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*eration*, 89 F.C.C. 2d 58 (1982), *appeal pending sub nom. Millicom, Inc. v. FCC*, No. 81-1404 (D.C. Cir.). For these reasons, the Court will not require the parties to modify the proposed decree specifically to address these concerns.

[270] As is true with respect to all of the principles and promises underlying the decree, they acquire meaning only through implementation. The Department of Justice may be expected, in the first instance, to see to it that there is appropriate implementation but, as described in Part XI *infra*, the Court also intends to see to it that all these principles and premises are actually carried out.

[271] The divested Operating Companies must file tariffs for their access services. Revenues collected pursuant to these tariffs will substitute for funds currently received by the Operating Companies under the division of revenue process, which allocates interstate toll revenues between the operating companies and the Long Lines Division. See Proposed Decree at Appendix B(B). Tariffs for intrastate interexchange access services will be filed with the state regulatory commissions, tariffs for interstate interexchange access services with the FCC. The proposed decree requires the Operating Companies to file tariffs which are cost-justified, but it does not limit the authority of the regulators to allocate costs pursuant to their regulatory policies. Thus, these tariffs may be set at a level which continues the current allocation of interexchange revenues. See also note 161 *supra*.

[272] Testimony of Irwin Dorros (November 24, 1981). For similar reasons, the provision permitting the Operating Companies to seek Court permission not to provide equal access services where, as a result of technologically

equal access to be achieved immediately or to be phased-in on a more expedited basis than is contemplated in the proposed decree.[273] Similarly, since the Bell System network is both vast and complex, a variety of approaches will in all probability be necessary to achieve equal access. Imposition by the Court of a single procedure applicable to all areas and all interconnection requirements is likely to create inefficiencies and impose added costs on the Operating Companies without achieving superior results.

The Court therefore finds that, generally speaking,[274] the means provided in the proposed decree to achieve equal access are adequate to protect the public interest.

B. Exceptions to Equality

The proposed decree contains some exceptions to the broad mandate of equality. These exceptions must be closely scrutinized to determine whether they will give AT&T an unjustified advantage over other carriers and thus obstruct the development of free competition.[275]

First. Long distance calls may presently be placed over the AT&T network by dialing ten or eleven digits while twenty-two or twenty-three digits are necessary to use the

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outdated switches "such access is not physically feasible except at costs that clearly outweigh potential benefits to users of telecommunications services," is also a justifiable deviation from absolute equality. Proposed Decree, Appendix B(A)(3).

[273] The decree does not, however, preclude the Operating Companies from providing equal access more expeditiously ... hey are capable of doing so.

[274] See Part B *infra*.

[275] Both AT&T and the Department of Justice cite this Court's ruling during an earlier phase of the *AT&T* proceedings with regard to interconnection to AT&T's network that "absolute equality of access to essential facilities . . . is not mandated by the antitrust laws." *United States* v. *AT&T*, *supra*, 524 F. Supp. at 1360. The Court's statement has reference to the access necessary to avoid antitrust liability. It is not necessarily the appropriate standard for evaluating an antitrust remedy. A remedy must impose the requirements reasonably necessary to open the relevant markets to competition. See Part II *supra*.

facilities of the other interexchange carriers. This substantial disparity in dialing convenience has had a significant negative impact on competition.[276] Under the proposed decree, this disparity will be drastically reduced, but some difference in the number of digits will remain: fourteen digits will be needed for the use of the facilities of a competing carrier while ten or eleven will be required for calls placed over the AT&T network.[277]

The reason given by the parties for this continued distinction is that full dialing parity is impossible without a change in the national area numbering plan. It appears, furthermore, that a change in that plan for all the telephone instruments in the United States would be both difficult and costly. When the FCC orders a revision in that plan — which it apparently has the authority to do at any time — the dialing parity which is in keeping with the equality principles of the proposed decree will in fact be achieved.

It is inappropriate for the Court to order such a change in advance of the FCC-required change-over; the difference in the required number of digits simply does not present an obstacle to competition sufficient to require the expense and effort involved in an early change in the plan.[278] This conclusion

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[276] Testimony of Bert C. Roberts, Jr. (April 27, 1981); Testimony of Jeffrey J. Kushan (May 1, 1981); Testimony of George Vasilakos (June 16, 1981).

[277] Proposed decree at Appendix B(A)(2). While the proposed decree states only that the "minimum number of digits" will be used, AT&T has indicated that fourteen digits will be required. See AT&T Reply Brief at 40.

[278] Somewhat similar considerations apply to the facilities-sharing question. After divestiture, AT&T will necessarily share facilities with the Operating Companies because the physical components of the nationwide network cannot be neatly divided between them. It would be inappropriate to require in the interest of symmetry, that the Operating Companies also to share facilities with the other interexchange carriers. This requirement would severely limit the Operating Companies' freedom to design their own networks and, as the number of carriers increases, such sharing could become physically impossible.

The decree appropriately ameliorates AT&T's advantages resulting from sharing by requiring the Operating Companies' charges to other carriers

is buttressed by the requirement in the proposed decree that the divested Operating Companies provide a service which will permit a subscriber to route his calls automatically to a single interexchange carrier other than AT&T. Appendix B(A)(2)(ii).[279] By means of this service, the subscriber will be able to use that carrier's network by dialing only the same ten or eleven digits that are required of an AT&T subscriber.

Second. Another exception to full equality is a provision which will permit the Operating Companies to provide billing services for only one interexchange carrier[280] which presumably will be AT&T.[281] Unquestionably, it would impose a considerable expense and administrative burden upon the Operating Companies to require them to provide billing services for all intercity carriers, and in the view of the Court this would not be in the public interest. Another alternative for the achievement of complete equality would be to prohibit the Operating Companies from providing billing services to any carrier (including AT&T). If this were done, AT&T would, of course, have to do its own billing.

The parties claim, and the Court agrees, that if AT&T had to establish its own billing system, it could do so only on the basis of a surcharge to its monthly telephone bills similar to

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to be equal to those charged to AT&T when that company's facility is close to an AT&T switch. See Appendix B(B)(3). This provision will remain in effect until 1991, by which time it is likely that AT&T's advantages will have been reduced by changes in the configuration of the local network. As to co-location in facilities constructed after divestiture, all carriers stand on the same footing: sharing is permitted, but not required.

[279] To be sure, the Operating Companies may impose a charge for this routing option, but not only would the charge most likely be minimal but it would also be temporary. As stated above, as soon as the FCC decides to change the national numbering plan, the entire problem will be resolved.

[280] An Operating Company would be free to provide billing services for more than one interexchange carrier; but it would not be required to do so.

[281] The divested Operating Companies will have the obvious incentive to provide billing services to the interexchange carrier with the greatest volume of calls so as to obtain the largest possible reimbursement for billing services.

the charges now imposed by interexchange carriers other than AT&T. Such a charge would be quite substantial,[282] and it would impose a significant burden upon telephone subscribers, particularly those — who are the majority of the users — whose monthly long distance bills are relatively small. It has been estimated that an additional charge of this type could double the long distance bills of many of these citizens.[283]

As indicated, the proposed decree resolves this problem by allowing the Operating Companies to engage in joint billing with AT&T. This solution would provide AT&T with an advantage over its competitors in two ways: (1) AT&T would have lower billing costs than its competitors;[284] (2) as the intercity carrier with access to Operating Company billing, AT&T might be perceived by the public as the "official" or approved intercity carrier.

As concerns the cost problem, the joint billing allowed by the proposed decree represents a reasonable trade-off: AT&T's competitors will suffer a slight competitive disadvantage, but vast numbers of consumers will benefit from lower costs as a consequence of joint billing economies. In the opinion of the Court, the public interest does not require that millions of telephone customers, particularly those with low usage (who presumably will be the less affluent) be in effect penalized by a fairly substantial extra charge in order to eliminate what to AT&T's competitors will not be a significant cost differential.[285]

The confusion that would be created in the public's mind by joint billing, and the probability that many consumers

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[282] It could be as much as five dollars per month per subscriber. Testimony of Irwin Dorros (November 24, 1981).

[283] Testimony of Irwin Dorros (November 24, 1981).

[284] AT&T would be required to reimburse the Operating Companies for the cost of billing. Proposed Decree at Appendix B(C)(2). However, this amount would presumably be less than that required if AT&T were to provide its own billing.

[285] The difference in cost is not likely to have a substantial effect on consumer choice for the high volume user which, for the present at least, appears to be the principal customer of AT&T's competitors.

would select AT&T by default simply because it appeared on the same bill with the monopoly Operating Company presents a more serious problem. However, that problem can be resolved, or at least sufficiently alleviated, without the drastic remedy of requiring AT&T to initiate its own billing operation, by allowing continued joint billing but requiring the Operating Companies to include on the interexchange portion of their bills a legend to the effect that

> This portion of your bill is provided as a service to AT&T. There is no connection between this company and AT&T. You may choose another company for your long distance telephone calls while still receiving your local telephone service from this company.

Therefore, the Court will not approve the proposed decree unless it is modified to incorporate this requirement. With this change, the degree of disparate treatment of interexchange carriers is permissible. To require more would be to place burdens upon the public not commensurate with the remaining slight disparities.

Third. The proposed decree would permit the Operating Companies to charge all interexchange carriers the same amount for access services during the interim period when AT&T still receives services superior to those provided to the other carriers. On its face, this provision appears patently anticompetitive. It will be difficult for AT&T's competitors to attract business if they are forced to pay the same amount in access charges as AT&T but receive inferior service. No persuasive justification has been given for this provision.[286] In fact, it seems clear that there should be no exception from the general rule that rates should vary depending upon costs. If therefore the cost of providing access services to the other carriers is less than that of providing access services to

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[286] AT&T states that lower costs could not be required because there was actually no difference in costs between the two types of access. See AT&T Reply Comments at 118. The Department of Justice contends that any such requirement would force the Court to value the diminished quality of access provided to AT&T's competitors. Department of Justice Brief at 35.

AT&T, the Operating Companies will have to file tariffs reflecting that difference,[287] and the Court will require that the proposed decree be modified accordingly.[288]

Fourth. Under Section I(a)(1) of the proposed decree the divested Operating Companies must be given whatever facilities are necessary to provide equal access to all interexchange and information service providers. There was considerable comment and controversy during the public interest proceedings over the use by the Operating Companies of so-called Class Four switches in the provision of such access.[289]

The switching of telephone calls in the nationwide network is divided into five functions depending upon the complexity of the switching tasks. However, a single physical unit will often perform more than one switching function. The Class Four function — the routing of toll calls — is generally regarded as a function of the interexchange network, but the physical switching unit which performs this function may be the most appropriate site for the interconnection between the Operating Companies and the other interexchange carriers.

There initially appeared to be some divergence of opinion between AT&T and the Department of Justice regarding the use by the Operating Companies of switches performing the Class Four function for the interconnection between the

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[287] If there is no difference in the cost of providing these services, it would be appropriate for charges to AT&T to be increased to reflect its higher quality connection. The Court will not impose this requirement because it lacks the expertise and flexibility to determine the amount of such a premium, but regulators remain free to insist on such a differential.

[288] The alternative chosen by the Court avoids the problems raised by the parties. See note 286 *supra*. It requires that the Operating Companies file tariffs which reflect lower rates for interexchange carriers other than AT&T only to the extent that the costs for such access are lower than the cost of access provided to AT&T. The Operating Companies will not be required to provide access services at below-cost rates, and the Court will not have to place a monetary value on the lower quality service.

[289] This matter is important because, in the view of the various intercity carriers, the Class Four switch provides the only gateway for toll quality transmission of interexchange traffic within the local exchange.

Operating Companies and AT&T's intercity competitors. The Department has always taken the position that these switches could be used for this purpose if the Operating Companies determined that this was the most efficient method for the provision of access equal in type and quality to that provided to AT&T. Response to Comments, pp. 89–92. AT&T's Reply Comments (at 107-08) suggested, however, that these switches are an integral part of AT&T's interexchange network and that the division between exchange and interexchange functions occurs at a different level of the network.[290] Ultimately, however, there was general agreement on the Department of Justice's formulation. Hearing on June 29, 1982 (Tr. 25201-03). The Court expects this principle to be implemented, both in the plan of reorganization and otherwise. See Part XI *infra*.

Fifth. AT&T's interexchange competitors have also urged the Court to withhold its approval of the decree until AT&T agrees not to seek increases in the level of Operating Company charges to interexchange carriers set by the FCC. See *Exchange Network Facilities (ENFIA)*, 90 F.C.C.2d ____ (No. 82-208, April 30, 1982), *review pending, MCI Telecommunications Corp.* v. *FCC*, No. 82-1554 (D.C. Cir.).

The ENFIA agreements were initially negotiated between AT&T and the other intercity carriers under the aegis of the FCC, and the Commission recently extended these agreements for an additional two years. *Exchange Network Facilities (ENFIA)*, 90 F.C.C.2d ____ (No. 82-180, April 14, 1982), *review pending MCI Telecommunications Corp.* v. *FCC*, No. 82-1553 (D.C. Cir.). AT&T filed new tariffs to implement that decision, but these tariffs were challenged by the other carriers. The Commission then suspended the tariffs and imposed an arbitrary interim rate to take effect until it determined the proper rate under the ENFIA agreements. It is clear from this history that the present rate is not within AT&T's discretion, but has, in fact, been set by the FCC and

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[290] According to AT&T, that division does not occur between the Class Four switching function and higher level switching functions but between local end office (Class Five) function and the Class Four function.

is under active review by the Commission and the courts. It would be improper for this Court to interfere with those proceedings.

For the reasons stated, the Court finds that, with the exceptions noted above, the equal access provisions of the proposed decree are adequate to protect the public interest.

## IX
## Division of Assets

Under the terms of the proposed decree, AT&T is required to divest itself of its Bell Operating Companies and to transfer to them (or to a newly-created entity or entities acting on their behalf) "sufficient facilities, personnel, systems, and rights to technical information to permit [them] to perform, independently of AT&T, exchange telecommunications and exchange access functions."[291] AT&T has proposed the following tentative procedure for effecting the reorganization required by this provision.[292] Initially, each Operating Company will establish three new subsidiaries, one for interexchange assets, another for customer premises equipment assets, and the third for directory advertising assets.[293] After the appropriate assets are transferred to these new subsidiaries,[294] each Operating Company will spin off ownership in the subsidiaries to AT&T by declaring a dividend of the new subsidiaries' stock. At the same time, AT&T will transfer to the Operating Companies, or to an entity owned by them,

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[291] Section I(A)1.

[292] Although under the proposed decree AT&T is not required to explain its procedures in this regard until it submits its plan of reorganization, it has announced this tentative proposal to inform the Court as well as other interested persons of its probable course of action.

[293] The Court has concluded that the Operating Companies may produce printed directory advertising. See Part VII *supra*. Establishment of the directory advertising subsidiary may therefore be unnecessary because those assets will be retained by the Operating Companies

[294] At the time of the transfer of assets, the Operating Companies may also transfer a portion of their debt issue to the new subsidiaries or to AT&T.

any additional assets necessary for the performance of their telecommunications and exchange access functions. Once this transfer of assets is completed, the Operating Companies will be reorganized into seven regional Operating Companies, and the stock in these seven companies will be spun off to the AT&T shareholders. See AT&T Reply Comments at 4-5; AT&T Brief at 61.

Opponents to the proposed decree claim that this method of dividing the assets is defective in several respects and they propose that the Court insist on the following modifications: (1) that AT&T be required to compensate the Operating Companies for assets removed from their balance sheets; (2) that the transfer of the assets be effected at market value rather than at net book value; and (3) that stronger procedures be established to prevent AT&T from manipulating the division of assets and liabilities to the detriment of the Operating Companies. Each of these issues is addressed below.

A. Compensation and Transfer of Assets

Those who claim that the Operating Companies should be compensated for assets transferred to AT&T misperceive both the law and the nature of the proposed reorganization. Under long-established general legal principles, the transfer of assets between a parent and its subsidiary is not an arm's length transaction for which compensation is required. Corporate law holds that such a transfer constitutes an intra-enterprise exchange for which compensation is not necessary.[296] The reason for this rule is simple: both before and

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[296] This rule applies regardless of the direction in which the transfer occurs. A transfer of assets from a parent to a subsidiary is treated as a contribution to capital for which the subsidiary is not required to provide consideration to the parent. See, *e.g.*, *United States* v. *Chicago, Burlington & Quincy Railroad Co.*, 412 U.S. 401, 405-06 (1973); *Abegg* v. *Commissioner*, 429 F.2d 1209, 1215-18 (2d Cir. 1970). The transfer of assets from a subsidiary to a parent is treated as a distribution or dividend for which likewise no compensation is required. See, *e.g.*, *Prescott, Ball & Turban* v. *LTV Corp.*, 531 F. Supp. 213, 214-15, 220 (S.D.N.Y. 1981). Apparently the only limitation on these rules is that a transfer may not impair the

after the transfer, the same shareholders maintain the same ownership interests in the same assets. The sole difference is that before the spin-off the shareholders' interests are represented by shares of stock in one company, while after the spin-off their interests are represented by shares in more than one company.

This general rule has routinely been applied to divestitures such as the one involved in these cases. For example, in *Western Union Telegraph Co.* v. *United States*, 267 F.2d 715 (2d Cir. 1959), Western Union, a carrier regulated under title II of the Communications Act, was ordered by the FCC to divest itself of its international telegraph operations as a prerequisite to a merger with another domestic telegraph company. In discussing how the company could comply with the FCC's order, the Court of Appeals stated that, should the divestiture be accomplished by a spin-off, there would be no "necessity of fixing a figure as [to] the value of the Western Union cables, since each Western Union stockholder would have the same pro rata interest in both Western Union landlines and Western Union cables following divestment, as prior to divestment."[296]

A similar approach was followed in *Pittsburgh Terminal Corp.* v. *Baltimore & Ohio Railroad, et al.*, No. 81-1674 (3d Cir. June 3, 1982). There, the C&O Railroad sought to develop its non-rail business free from restrictions imposed by the Interstate Commerce Commission, and it therefore undertook a reorganization plan similar to the one proposed by AT&T. C&O owned almost all of the common stock of the B&O

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rights of interested third parties, such as creditors. See, *e.g.*, *Superintendent of Insurance of New York* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 12 (1971); *Pepper* v. *Litton*, 308 U.S. 295, 307 (1939); *Hanraty* v. *Ostertag*, 470 F.2d 1096, 1099 (10th Cir. 1972); *Guaranty Trust Co. of New York* v. *Grand Rapids G.H.&M. Ry. Co.*, 7 F. Supp. 551 (W.D. Mich. 1931), *mod. on reh.*, 85 F.2d 331 (6th Cir. 1936).

[296] 267 F.2d at 719-20. The fact that Western Union ultimately decided to accomplish the divestiture through a sale rather than a spin off (see *Western Union Telegraph Co.*, 30 F.C.C. 323 (1961)) in no way undermines the Court of Appeals' general characterization of a spin off as a compensation-free transfer.

Railroad, a corporation which had both rail and non-rail assets. To remove the non-rail assets, B&O created the Mid-Allegheny Corporation (MAC) as a new wholly-owned subsidiary, and it transferred to MAC all of the B&O non-rail assets in exchange for MAC stock. It then spun off ownership in MAC to its parent, the C&O, by declaring a dividend of MAC stock. At no time during the reorganization was any valuation or compensation procedure involved or required.[297] Just as it was unnecessary for the C&O to "pay" the B&O for the transfer of ownership of the non-rail assets, so, too, it is unnecessary for AT&T to compensate the Operating Companies for the transfer of those assets which are not needed for the performance of the local exchange and exchange access functions.[298]

It is worth noting in this connection that the state regulators, who are the principal opponents of the reorganization method prescribed by the proposed decree, have traditionally treated AT&T and the Operating Companies as a single enterprise rather than as separate corporations dealing with each other at arm's length.[299]

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[297] Although the Court of Appeals reversed the District Court's finding that holders of convertible debentures were not entitled to notice of the plan for reorganization, it did not in any way question the propriety of the corporate reorganization itself or the basic manner in which it was carried out.

[298] See also, *United States* v. *El Paso Natural Gas Co.*, 358 F. Supp. 820 (D. Colo. 1972), *aff'd*, 410 U.S. 962 (1973), where the court upheld a reorganization whereby El Paso transferred all of its pipeline assets at net book value to a newly-formed company in exchange for the new company's stock, then sold twenty percent of this stock, placed the remainder in a voting trust, and distributed participation certificates in the voting trust to El Paso shareholders, without any compensation between El Paso and the new company; and *United States* v. *United Fruit Co.*, 1958 Trade Cas. ¶ 68,941 (E.D. La. 1958), where the court ordered the defendant either (a) to create a new corporation capable of competing with the defendant and then to distribute the new company's stock to defendant's shareholders or (b) to sell sufficient assets to a third party in order that this third party could compete with the defendant.

[299] The debt-equity ratio that is used by state regulators in calculating rates of return, for example, is not that for the individual Operating

Opponents of the settlement rely on *Democratic Central Committee* v. *Washington Metropolitan Transit Commission*, 485 F.2d 786 (D.C. Cir. 1973), as allegedly requiring a different result.[300] To be sure, the Court of Appeals held in that case that capital gains realized on the disposition of assets do not automatically flow to the firm's investors but instead inure to the benefit of ratepayers,[301] and opponents of the proposed decree conclude from that holding that AT&T must compensate the Operating Companies and thus, indirectly, local ratepayers. But there is a crucial difference between the disposition of assets that was involved in that case and the transfer of assets proposed here. In *Democratic Central Committee*, the assets were taken out of operation and out of the rate base; obviously, when this occurred a gain was realized and it then became necessary to determine to

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Company being directly regulated but rather the consolidated debt-equity ratio for the entire Bell System. The reason for this approach is clear: the regulators recognize that the debt ratio of each Operating Company is the result of AT&T's distribution of its debt and equity capital among the entities in the Bell System, and that the consolidated ratio is therefore a better reflection of the Operating Company's actual financial condition. As the New York Public Service Commission said:

> Using a consolidated capital structure is correct here because AT&T and its subsidiaries conduct their financings on a centralized, coordinated basis, which leaves largely to chance the market conditions prevailing when a particular subsidiary is scheduled to issues securities.

*New York Tel. Co.*, 23 P.U.R.4th 554, 562 (N.Y. Pub. Serv. Comm'n. 1977). See also, *Chesapeake & Potomac Tel. Co.*, 10 P.U.R.4th 211, 218 (Md. Pub. Serv. Comm'n. 1975); and *New England Tel. & Tel. Co.* 95 P.U.R.3d 71, 83 (N.H. Pub. Util. Comm'n. 1972).

[300] See also *Bebchick* v. *Washington Metropolitan Area Transit Commission*, 485 F.2d 858 (D.C. Cir. 1973).

[301] Said the court (485 F.2d at 821):

> Transit's farepayers have long been saddled with the burdens incidental to the properties in issue while they remained in operating status. Theirs were the expenses of ordinary maintenance and depreciation, and the risks of loss from casualty and obsolescence, associated with those properties . . . . And Transit's investors have profited, not only from these arrangements of burdens, but also from favorable treatment of the operating assets in other ways. By our assessment, these circumstances tip the scale in favor of Transit's farepayers, so much as to earn for them the gains beyond the shadow of a doubt.

whom the benefit of that gain should inure.[302] But no assets are here being removed from public service: the same assets will continue to be used to provide the same services to the same ratepayers, and the assets will remain subject to the same ratemaking jurisdictions of the same regulators.[303]

There can thus be little doubt that, as a matter of the law, the transfer of assets contemplated by the proposed decree is no more and no less than the usual kind of intra-enterprise exchange for which no compensation is necessary.

This result also makes sense from a practical point of view, for several reasons.

In the first place, were the Court to require AT&T to compensate the Operating Companies for the removed assets, it would in essence place AT&T in the anomalous position of having to repurchase assets it already owns. There is no warrant whatever for such a course. Second, a requirement that AT&T pay the Operating Companies for the transferred assets — which are valued at many billions of dollars — would produce a severe, if not crippling, financial strain on AT&T. Third, payment of compensation would convert what would otherwise be a tax-free transfer into a taxable exchange, thus exposing the Operating Companies to possibly

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[302] See also *Bebchick* v. *Washington Metropolitan Area Transit Commission*, *supra*, 485 F.2d 858.

[303] The FCC concurs in this position. It has advised the Court that "implementation of the proposed decree will not inevitably produce any retirement from service" of any of the Operating Companies' assets. Topic 4 Brief of FCC at 7. The proposed decree will not in any way disturb the authority of regulators to determine the proper valuation of assets regulated by their jurisdictions. For example, assets used to provide intrastate interexchange service will not be deregulated by the decree but will remain under regulation by the state commissions. These assets may simply be owned by a different corporate entity.

It is irrelevant to these proceedings that certain assets, such as customer premises equipment, may eventually be removed from public service because of eventual deregulation under the FCC's *Computer II* decision or other regulatory action. If valuation problems arise as a result of the retirement of these assets regulatory decisions; they would not stem from the proposed decree.

billions of dollars in federal and state tax liabilities. See 26 U.S.C. §§ 368(a)(1), 368(c).[304] Finally, if the transfer of assets were treated as a sale negotiated at arm's length, it is entirely possible that AT&T would decline to purchase unattractive Operating Company assets, deciding instead to purchase more up-to-date or efficient property from some third party. Since the Operating Companies would still be obligated under the terms of the proposed decree to dispose of these assets, they could conceivably be forced to sell them at greatly reduced prices — if they could sell them at all — leaving ratepayers with the obligation to produce additional revenue to compensate for the deficiency.

B. Book Value vs. Market Value

Related to the question of compensation is the question whether the transfer of assets should occur at net book value or at market value. It is not necessary to decide whether, as a matter of law, all transfers of property between a parent and its subsidiary must be effected at book value; what is clear is that, in this case, net book value is the appropriate standard.[305]

Since the mid-1940s, regulators have almost universally relied on net book, rather than market, value for ratemaking purposes. See, *e.g. Federal Power Commission* v. *Hope*

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[304] Treas. Reg. § 1.1002-1(c) (1956) holds that the underlying assumption in providing for tax-free reorganizations is that "the new property is substantially a continuation of the old investment still unliquidated; and, in the case of reorganizations, that the new enterprise, the new corporate structure and the new property are substantially continuations of the old still unliquidated." See, *e.g.*, *United States* v. *Adkins-Phelps, Inc.*, 400 F.2d 737, 740 (8th Cir. 1968); *Commissioner* v. *Wilson*, 353 F.2d 184, 186 (9th Cir. 1965). This assumption obviously would not apply if AT&T were required to pay for the assets. The suggestion of some who object to the proposed decree that this tax liability could be avoided by an amendment of the current tax laws is entirely unpersuasive. The Court applies the laws as they now exist, not as they may some day be.

[305] There is a serious question whether a compensation-free transfer could realistically be effected other than at net book value. Further, market valuation would probably entail a number of undesirable post-divestiture consequences (*e.g.*, calculation of the rate base, taxation of the exchange).

*Natural Gas*, 320 U.S. 591 (1944); *Re Southern Bell Tel. & Tel. Co.*, Docket No. 78-353-C, Order No. 79-90, 30 P.U.R. 4th 263, 271 (S.C. Pub. Serv. Comn. 1979); *Re New York Tel. Co.*, Case 25155, 84 P.U.R.3d 321, 339 (N. Y. Pub. Serv. Comn. 1970); *Re Pacific Tel. & Tel. Co.*, Case No. 7409, 53 P.U.R.3d 513, 543 (Cal. Pub. Utils. Comn. 1964). This method of valuation has also consistently been used in cases involving the transfer of assets between different Bell System entities, regardless of whether the transfers were relatively insignificant (such as those involving switching equipment or other properties) or whether they involved the total reorganization of an Operating Company (such as the separation of South Central Bell from Southern Bell or the separation of Pacific Northwest Bell from Pacific Bell).[306]

Apparently the primary reason for the general preference of net book value over market value is that it is readily ascertainable,[307] while market value is much difficult to compute.[308] That reasoning has special applicability here. If market value were to be used in the instant case, valuation proceedings would have to be conducted for all of the billions of dollars worth of AT&T's assets.

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[306] See, *e.g.*, *Application of Illinois Bell Tel. Co.*, Docket 78-0121 (Ill. Commerce Comn., April 19, 1978) (sale of Illinois Bell switching equipment to AT&T at net book); *Application of Mountain States Tel. & Tel. Co.*, Docket 3999 (Tex. Publ. Utils. Comn., Nov. 13, 1977) (sale by Mountain Bell of plant to Southwestern); *Re Pacific Tel. & Tel. Co.*, Docket No. U-F-2286, 39 P.U.R.3d 132, 135-36 (Oregon Pub. Utils. Comn. 1961).

[307] It is computed simply by using the original cost and depreciation.

[308] See, *e.g.*, *Re Southern New England Tel. Co.*, Docket No. 10054, 42 P.U.R.3d 310, 320 (Conn. Pub. Utils. Comn. 1962); *Re New York Tel. Co.*, 91 P.U.R. (n.s.) 231, 257 (N. Y. Pub. Serv. Comn. 1951). Moreover, in a regulated firm, there is the additional problem of an interdependence between rates and market value. Specifically, the market value of an asset depends upon the revenue it generates, but in a regulated industry the amount of revenue is dependent on the level of rates set by regulators. As stated by the Supreme Court in *FPC* v. *Hope Natural Gas*, *supra*, 320 U.S. at 601:

> The heart of the matter is that rates cannot be made to depend upon "fair value" when the value of the going enterprise depends on earnings under whatever rates may be anticipated.

AT&T has correctly pointed out the overwhelming nature of this task by referring to the extensive, complex, and lengthy valuation proceedings in the *Conrail* case.[309] Valuation proceedings for the Bell System assets would necessarily be even more complicated and unmanageable than those involving Conrail, for the value of AT&T's assets is not only substantially greater than that of the Conrail assets, but the court there had at least the advantage of valuating assets from bankrupt estates.[310] In contrast, the Bell System is an ongoing business, and market dynamics would therefore be of much greater significance here than they were in *Conrail*.[311]

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[309] The Regional Rail Reorganization Act of 1973 mandates the transfer of assets from the estates of certain bankrupt railroads to the newly formed Conrail Corporation, and a Special Court was appointed to determine the value of the transferred assets. 45 U.S.C. §§ 743, 746. Despite the fact that the valuation proceedings for these assets began in the mid-1970s, they have yet to be completed. Indeed, the almost insuperable obstacles surrounding such proceedings led Judge Friendly to observe in 1977:

> . . . we would be remiss if we did not advise the parties and also the lawmakers of our fears as to the length and cost of these proceedings if they are carried to a conclusion under the charter that has been given us, even with the simplifying limitations we have here imposed. Nearly four years have elapsed since the Rail Act was adopted and a year and a half have gone by since the conveyances. Yet despite earnest sincere efforts by all concerned, we are only at the start of the valuation problem.

*Matter of the Valuation Proceedings under Sections 303(c) and 306 of the Regional Rail Reorganization Act of 1973*, 445 F. Supp. 994, 1045 (Sp. Ct. 1977). Despite the fact that over eighty percent of the case was settled by the parties, the Special Court concluded the rail-use phase of the valuation proceedings with the issuance of its 200 page opinion only in late 1981. See *Matter of the Valuation Proceedings*, 531 F. Supp. 1191 (Sp. Ct. 1981). The nonrail-use phase of the proceedings has only begun: opening briefs will not be filed until October 2, 1982, and oral argument is not scheduled until January 4, 1983. *Matter of the Valuation Proceedings*, Misc. No. 76-1, Order (Sp. Ct. July 6, 1982).

[310] Thus, the suggestion by some that the valuation process could be completed within six months (see Topic 4 Brief of People of California, *et al.*, at 35) is wholly unrealistic; and those who make these proposals are ultimately driven to the conclusion that the entire divestiture must be abandoned as impractical. Reply Brief of People of California *et al.* at 9.

[311] The suggestion that the pitfalls of the *Conrail* case could somehow be avoided by allowing the state regulatory bodies to value the assets may

The Court finds that there is no justification for abandoning the well-established practice of valuing assets at net book for purposes of the proposed decree.[312]

C. The Division of Assets and Debts

It has further been suggested by a number of interested persons that AT&T might manipulate the actual division of assets and liabilities to the detriment of the Operating Companies.

Initially it may be observed that AT&T has the responsibility, separate and apart from the proposed decree, to insure that the Operating Companies are spun off as financially viable entities. As their majority, and in some cases sole shareholder, AT&T has the fiduciary duty to protect all those with interests in these Companies, including creditors. See *Pepper* v. *Litton*, 308 U.S. at 306; see also *Superintendant of Insurance* v. *Bankers Life*, *supra*, 404 U.S. at 12; *Hanraty* v. *Ostertag*, *supra*, 470 F.2d at 1099. Other shareholders are protected by similar principles. See *Kamin* v. *American Express Co.*, 383 N.Y.S.2d 807, 812, *aff'd*, 387 N.Y.S.2d 993 (Ct. App. 1976); *United Copper Securities Co.* v. *Amalgamated Copper Co.*, 244 U.S. 261, 262–64 (1917); *Lewis* v. *Anderson*, 615 F.2d 778, 782 (9th Cir. 1979); *Rosengerten* v. *International Tel. & Tel. Corp.*, 466 F. Supp. 817, 822 (S.D.N.Y. 1979); *Auerbach* v. *Bennett*, 419 N.Y.S.2d 920, 927 (Ct. App. 1979). Antitrust principles, too, impose a duty on the divesting corporation to establish the newly-divested business with a sound financial structure. *Utah Public Service Commission* v. *El Paso Natural Gas Co.*, 395 U.S. 464, 470 (1969); *Ford Motor Co.* v. *United States*, 405 U.S. 562 (1972); *Maryland Milk Producers' Assn.* v. *United States*, 362 U.S. 458 (1960). It should not lightly be assumed that AT&T's

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readily be rejected. To permit forty-nine different forums to conduct forty-nine different proceedings would only exacerbate, not diminish, the problems.

[312] This decision of course in no way affects the authority of regulators to use a different standard in valuing assets within their jurisdiction for ratemaking purposes.

managers will violate this trust and expose themselves to substantial liability.

Beyond that, the Court is satisfied that, with some modifications, there are adequate safeguards to protect against abuse.

Perhaps the most important guarantee against improper manipulation is the one included in the proposed decree itself: that assets will be divided according to the functions they perform.[313] Thus, the Operating Companies will receive those assets necessary to perform exchange telecommunications and exchange access functions, and the remaining assets will be held by AT&T. There appears to be wide agreement that at least eighty percent of the assets may be readily identified and assigned on this basis. With respect to this portion of the assets it is therefore necessary only to ensure that the functional division will actually be carried out. A number of measures will serve this purpose.

First, in addition to its own review and approval of the division of assets, the Department of Justice has invited federal and state regulatory bodies as well as AT&T's competitors and other interested persons to examine the distribution of assets provided for in the plan of reorganization. See, *e.g.*, Department of Justice Response to Comments. at 15–21; Tr. 25,402. If it should appear that assets have been improperly assigned, the errors may be brought to the Department's attention, and it will then presumably take corrective action. Second, should the Operating Companies find, once they are divested, that they lack sufficient assets to perform their obligations under the decree, they may petition the Court under Section VII of the proposed decree for necessary relief. Third, the Court will continue its supervision of the decree, and it will in particular seek to ensure that the plan of reorganization is consistent with the decree's principles, including the principles which govern the distribution of assets. See Part XI *infra*. In view of the relatively ministerial nature of the task, these safeguards should be

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[313] Section I(A)2.

fully adequate to the ensure proper allocation of the single-function assets.

A more substantial problem is presented by the valuation of the remaining twenty percent of the assets — those representing multifunction facilities (that is, facilities providing functions for services rendered both by AT&T and by the Operating Companies). These include such important assets as land and buildings, cables, central office switching facilities, warehouses, underground conduit, manholes, and toll terminals. The proposed decree provides in Section I(A)2 that "there shall be no joint ownership of facilities, but appropriate provision may be made for sharing, through leasing or otherwise, of multifunction facilities so long as the separated portion of each BOC is ensured control over the exchange telecommunications and exchange access functions."

The parties appear to differ in their interpretation of this provision. The Department of Justice states that the entity which makes predominant use of a facility will "generally" be entitled to its ownership.[314] AT&T, on the other hand, interprets this provision to mean that multifunction facilities will be allocated on the basis of "reasonable, neutrally applied criteria," without, however, specifying what these criteria would be.[315]

In the view of the Court, it is essential that the predominant use test proposed by the government be applied to multifunction assets. Like the functional test that will be used generally in the division of assets, the predominant use test is a clear-cut standard which minimizes subjective factors and thus the potential for improper manipulation of the allocation process. Moreover, such a test provides the Court with a readily reviewable standard should the division of these facilities be called into question.[316] By contrast, the test

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[314] Department of Justice Brief at 60.

[315] AT&T Brief at 88; AT&T Reply Brief at 92. AT&T acknowledges only that predominant use will be "a major criterion" in allocating ownership of the assets. Reply Brief at 92.

[316] When this test is coupled with the provision allowing for cost-based

proposed by AT&T is vague and it leaves to that Company's management a vast amount of discretion precisely in the area where there is the most incentive for abuse. For clearly, it would be to AT&T's interest to select for itself assets of high utility and relatively low book value, while leaving to the Operating Companies the more costly but outmoded equipment, the least attractive real estate, and the under used plant. The possibility that AT&T will act on these incentives is too real to leave the distribution of the assets to AT&T's discretion under a "reasonable criteria" standard.

Because the predominant use test is an essential ingredient for the fair and successful implementation of divestiture, the Court will require in the public interest that the proposed decree be modified explicitly to incorporate that test. Such inclusion will permit the Court to oversee with some assurance of success that the division of assets will be fairly carried out.[317]

Questions have also been raised regarding the appropriate debt-equity ratios to be assumed by the Operating Companies and AT&T. AT&T has stated that it is willing to divest the Operating Companies with debt ratios of approximately forty-five percent and to assume its representative share of the outstanding debt, by assuming debt issues that have interest rates and maturities which reflect the average terms of the particular Operating Company debt.[318] The Department of Justice endorses AT&T's statement of intentions adding, however, that the Operating Companies should be left with debt issues that reflect terms and conditions comparable to the debt held by the Bell System as a whole. Department of

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leasing, it will assist in the division of multifunction facilities in a manner that is fair to both AT&T and the Operating Companies. Section I(A)2.

[317] The required modification will provide the necessary flexibility in the event it is determined that in certain instances the predominant use test is inappropriate. See Part XII *infra*.

[318] AT&T has stated that it will do so either by assuming a proportion of each debt issue or by assuming all of certain debt issues that have appropriate rates and maturities. See AT&T Reply Comments at 76-80; AT&T Brief at 90; AT&T Reply Brief at 95-96.

Justice Response to Comments at 30; Department of Justice Brief at 62.

The Court sees no reason for rejecting the parties' plan. The suggestions made by various third persons[319] do not differ significantly from those submitted by the parties, and they have certainly not shown that the parties' proposals are at all unreasonable. However, as is true with respect to several other matters, the Court considers that its Tunney Act responsibilities require it to demand more of the parties on subjects which have significant public interest aspects than statements of intentions embodied in briefs or written comments, or made during oral argument. Accordingly, the Court will require that the proposed decree be modified to incorporate the forty-five percent debt ratio[320] and the government's and AT&T's representations with regard to the quality of the Operating Company debt,[321] to the end that on the basis of such a modification the Court will be in a position, if necessary, to insist that the statements of intention of the parties are actually implemented.

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[319] These persons have proposed different alternatives: some contend that no Operating Company should have a debt ratio over 50 percent; others that the Operating Companies should be spun off with the same debt ratio they had before divestiture; still others argue that, regardless of what ratio is chosen, it should be the same for all the Operating Companies so as to ensure that after divestiture they will have equal opportunities to attract new financing.

[320] Pacific Telephone currently has a substantially higher debt-equity ratio (at about 75 percent) due in large part to the actions of California's regulators. The Court will not require AT&T to reduce Pacific Telephone's debt to 45 percent, but will accept a reduction of Pacific's debt to around 50 percent. This 50 percent ratio appears to be acceptable to the State of California. See Topic 4 Brief of the State of California at 38.

[321] In actual practice, there may be a distinction between the Department of Justice's proposal regarding the quality of the debt and that of AT&T. The Court expects that the plan of reorganization will provide each Operating Company with a debt portfolio that reflects the terms and conditions comparable to the debt held by the Bell System as a whole unless it can be shown that, with respect to a particular Operating Company, its own current debt provides a more equitable basis. In the event of a dispute, the chief executives of the new regional Operating Companies may be heard regarding this subject.

The Court is satisfied that the provisions in the proposed decree, as modified, along with traditional corporate principles, provide a sound framework for the division of the assets and of the debt. The interests of the Operating Companies, including those of its creditors and future shareholders, will be protected by the functional division of assets, the predominant use test for multifunction facilities, and the guidelines established for the division of the corporate liabilities. The procedures established for the review of the reorganization plan and its implementation will further help to ensure that the principles of the decree be carried out. See Part XI *infra*. Finally, the fact that AT&T has a fiduciary obligation, separate and apart from the decree, to approach the divestiture in good faith and to protect the interests of all involved will further help to guarantee that the division of assets will be carried out in the public interest.

## X

## Special Provisions and Concerns

A number of those who have commented on the proposed decree have raised special problems which are outside the scope of the general categories discussed above. The Court has considered all of the issues presented by these comments, and it finds that none constitutes grounds for withholding approval of the proposed decree. Five of the most important concerns are discussed below.

### A. Department of Defense Concerns

The comments of the Department of Defense indicate continued opposition to the concept of the divestiture of the Operating Companies, and they suggest that the Department prefers an integrated AT&T as a defense asset.[322] These

[322] Thus, the Department states that the features of the integrated Bell System "have led us to express our view that divestiture of major components of the Bell System particularly structural separation between the local exchange and interexchange functions, would adversely impact system integrity and the Bell System's current ability to promptly provide emergency communications support and restoration." Department of Defense Comments at 16; see also, *id.* at 24.

comments ignore the testimony adduced during the *AT&T* trial, much of it by witnesses with close ties to the Defense Department,[323] to the effect that, far from relying directly or even primarily on AT&T, the Department and its allied agencies have in recent years increasingly placed their trust in their own, or in other non-AT&T sources for their communications needs.[324] In any event, the Department now appears to recognize that its stated interests cannot override the government's basic divestiture decision, and it thus concentrates the bulk of its remarks on recommendations for achieving a telecommunications network that will be effective for national defense and emergency purposes once divestiture is accomplished.

Some of these recommendations require no action by the Court because they address matters of definition;[325] request the resolution of conflicts that are theoretical at best;[326] or discuss problems which have little to do with the settlement.[327] However, there is one series of comments that has substantial merit.

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[323] *E.g.*, Secretary of Defense Harold Brown (December 17, 1981); former Deputy Secretary of Defense David Packard (November 6, 1981); Gerald P. Dineen, former Deputy Undersecretary of Defense for Research and Engineering (December 16, 1981); and former Air Force general Lee M. Paschall (November 6, 1981). All these individuals were called as witnesses on behalf of AT&T.

[324] See, *e.g.*, the trial testimony of Dr. Dineen at Tr. 24538-39; General Paschall at Tr. 19699-711. Bell Laboratories continues to be an important supplier of sophisticated equipment to the Defense Department; however, the divestiture does not disturb its relationship to AT&T.

[325] *E.g.*, whether such concepts as "emergency" and "customer premises" are adequately defined.

[326] The proposed decree provides (in Section I(C)) that until 1987, AT&T shall provide research and development services to the Operating Companies on a priority basis, while under the Defense Production Act, 50 U.S.C.A. App. § 2061 *et seq.*, priorities may be assigned to contracts necessary or appropriate to the national defense. There is no reason why AT&T cannot satisfy both requirements.

[327] The Department complains (Comments at 27–31) that inter-exchange carriers, but not customers of telecommunications carriers, are given the benefit of the provisions which prohibit the Operating Companies from

The Department notes that Section I(B) of the proposed decree directs the Operating Companies to "provide, through a centralized organization, a single point of contact for coordination of BOCs to meet the requirements of national security and emergency preparedness," and it correctly observes that there is no elaboration on the purpose and scope of the "single point of contact" requirement. The Department focuses on five specific areas in this regard, three of which constitute legitimate subjects of concern: (1) the lack of a requirement in the proposed decree that the Operating Companies commit specific resources to this point of contact; (2) the question of funding and regulatory treatment for this facility; and (3) the degree of authority the facility would possess to instruct the Operating Companies to cooperate in emergency situations, particularly in regard to the assignment to each other of necessary resources.[328] The Court expects that AT&T's plan of reorganization will resolve these issues in a manner which satisfies the Defense Department's legitimate needs without impairing the basic antitrust purposes of the judgment.[329]

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discriminating in providing access. The proposed decree addresses a real problem: that the Operating Companies, because of their past ties to AT&T, might give special consideration to their former parent. It is difficult to believe that the Operating Companies would have an incentive to discriminate against their customers, particularly large customers such as the United States government.

[328] A fourth recommendation is that AT&T be authorized and required to participate in the planning, administration, and operation of this "single point of contact" or any centralized administrative entity the Operating Companies may establish. The proposed decree quite properly rejects that concept since it would be antithetical to the basic theory and purpose of the decree. Similarly unacceptable, and for the same reasons, is the Defense Department's request that the Operating Companies be permitted to engage in coordination beyond the needs of national security and emergency preparedness.

[329] Since the subjects covered in this section of the opinion concern intragovernmental matters, the Court assumes that accommodations can be worked out between the Department of Justice and the Department of Defense without the need for specific modifications of the decree. However, the Department of Defense will be afforded an opportunity, following the submission of the reorganization plan, to submit further comments to the

B. Interests of AT&T Employees

The Communications Workers of America[330] submitted both comments and briefs, stating that it favors approval of the proposed decree. Its primary interest is in continued national bargaining in telecommunications following the reorganization of AT&T, and it requests that the proposed decree explicitly provide that nothing therein will preclude such a procedure. In the view of the Court, there is no need for such a modification. There is nothing in the proposed decree or in general principles of law which would preclude or interfere with such bargaining, and there accordingly is no reason whatever why, following the entry of the decree and the reorganization, such bargaining cannot continue as in the past.

The Communications Workers have further advised the Court that in August 1980 the union entered into a memorandum of understanding with AT&T[331] which specified that employees of the Bell System who were transferred to separate AT&T subsidiaries or affiliates would be entitled to certain protections.[332] Again, it is clear that, notwithstanding the separation of the Operating Companies from the Bell System, there will be no obstacle either to adherence by any of the restructured segments of the Bell System to the terms

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Court, should it be dissatisfied with the arrangements made by AT&T and the Department of Justice.

[330] This labor union represents over 500,000 employees of the Bell System, or 51 percent of all of the System's employees, in addition to over 70,000 employees in other telecommunications companies.

[331] This was done in anticipation of the establishment of separate subsidiaries or affiliated entities, presumably by requirement of the FCC.

[332] These include the preservation of wages and net credited service of transferred employees for five years after the transfer; no reduction of pension, health, or other benefits as a result of the transfer; payment of reasonable travel and moving expenses for transferred employees; continued application of the collective bargaining agreement to these employees; preferential rehiring rights; advance notice to the union of any work group transfer; and continued recognition by the subsidiaries or affiliates of the Communications Workers of America as the exclusive bargaining representative of transferred employees.

of existing collective bargaining agreements or to their abiding by such memoranda of understanding as may have been or may hereafter be negotiated with the union.[333]

The purpose of the divestiture is to establish conditions which will prevent the type of anticompetitive activities which the government has charged in its complaints in the two lawsuits presently before the Court. These activities, and hence the settlement of the lawsuits, do not involve AT&T's labor relations and, more particularly, they have nothing to do with the Communications Workers of America or its relationship with the Bell System. See also, 15 U.S.C. § 17; 29 U.S.C. § 52. It follows that the union, on the one hand, and AT&T, and the divested Operating Companies, on the other, will be entirely free to arrange their mutual labor relationships as the Bell System and the union did in the past, irrespective of the structural changes that may be brought about by the decree.

C. Prima Facie Effect of the Decree in Private Litigation

Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a) provides that

> a final judgment . . . rendered in any . . . proceeding brought by . . . the United States under the antitrust laws to the effect that a defendant has violated such laws shall be prima facie evidence against such defendant [in a private action] as to all matters respecting which said judgment would be an estoppel as between the parties thereto.[334]

Several parties argue that they are entitled to the benefits of the presumption established by this provision in any suits they may have brought or may hereafter initiate against

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[333] Obviously, the divested Operating Companies and other successor AT&T entities may subsequently negotiate superseding collective bargaining agreements with the majority representatives of their employees.

[334] The statute goes on to provide that it does not apply to consent judgments entered before any testimony is taken.

AT&T charging conduct similar to that involved in the government's *AT&T* action presently before this Court.[335]

AT&T presents two arguments in opposition to this suggestion.[336]

First, it contends that the proposed decree is only a modification of the 1956 decree, and that, since that decree was entered before any evidence had been taken in the *Western Electric* case, section 5(a) of the Clayton Act does not apply by its own terms. See note 334 *supra*. The Court has rejected this highly artificial argument in other contexts (see Part I *supra*) and it again rejects it here. The parties may not escape either the mandate of the law or the possibility of liability by the transparent device of attaching their settlement to an old, largely dormant case rather than to an action that is currently in litigation, especially where almost the entire settlement relates to the current lawsuit.

AT&T's second argument has considerably more merit. As indicated, the statute establishes a presumption usable in private litigation only on the basis of a judgment "to the effect that a defendant has violated [the antitrust] laws." Not only does the proposed decree fail to include a finding or admission that AT&T has violated these laws,[337] but Section III of the decree specifically provides that the judgment "shall

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[335] Other parties suggest that the Court should not enter the judgment without first making specific findings that might be used by private parties in subsequent litigation. There is no warrant for such findings. Although the vast majority of the evidence has been adduced, the trial has not been concluded, and the Court would therefore not be justified—absent a waiver by the parties or their refusal to produce additional evidence—to make findings of fact. See, *e.g.*, *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968); *Emich* v. *General Motors Corp.*, 340 U.S. 558, 566–72 (1951).

[336] The Department of Justice appears to take a position only on the second of AT&T's arguments. See Department of Justice Response to Comments at 134–36.

[337] Likewise, nothing in this opinion is intended to constitute a finding of violation of the antitrust laws.

[not] constitute any evidence against, an admission by, or an estoppel against any party or [Operating Company]." In view of that unequivocal provision, it would appear to this Court that the judgment herein would not have a prima facie effect in private litigation. However, as the Department of Justice correctly points out, the ultimate decision with respect to this issue must rest with the court in which such litigation may be brought. Response to Comments at 136. The Court will therefore decline to enter any specific decision or finding regarding this subject.

D. Conflict with Federal Regulation

Several interested parties have suggested that there may be a conflict between the proposed decree and regulation by the Federal Communications Commission, and that the decree therefore should not be entered unless and until the Commission has given its formal approval.

It is true that FCC certificates are required under the Communications Act for a number of transactions necessary to implement the divestiture. See 47 U.S.C. § 214(a), 221(a), 310(d). It is not likely, however, that a controversy will actually arise with respect to any of these matters. The FCC has already declared that "the basic settlement appears to be fair and reasonable," and it has suggested throughout its participation in these actions that there will be no difficulties with regard to implementation. Brief of FCC as amicus curiae at 9. The Supreme Court has admonished the lower courts not to adjudicate potential conflicts between an antitrust decree and a federal regulatory statute until there is a concrete case or controversy in that respect. *Otter Tail Power Co.* v. *United States*, 410 U.S. 366, 377 (1973). Accordingly, the Court need not and will not decide specific questions of possible conflict at this time.

The Federal Communications Commission has suggested in a somewhat similar vein that the decree should accommodate the federal regulatory scheme by the addition of a clause modeled on the so-called *Terminal Railroad* proviso. In *United States* v. *St. Louis Terminal*, 224 U.S. 383 (1912)

the Supreme Court directed the entry of a decree which, *inter alia*, changed some billing practices and eliminated a special charge for certain types of rail traffic. Because of a concern that these provisions created a potential conflict with Interstate Commerce Commission regulation of interstate rail transportation, the Court ordered that a proviso be attached to the effect that the decree did not affect the ICC's powers. 224 U.S. at 412. The District Court entered a decree in conformity with the Supreme Court directive (see *Terminal R.R. Ass'n* v. *United States*, 266 U.S. 17, 25 (1924)); and it is a clause paralleling that decree that the FCC requests here.

It is not at all clear why the FCC asks for inclusion in the decree in these cases of the *Terminal Railroad* proviso. The Commission acknowledges that

> The addition of such a provision would not change the substance of the proposed [decree]. There is no reason to suppose that either party to the settlement ever intended to affect any Commission power. Moreover, the failure to add such a proviso would not expand the court's power or contract the Commission's power.

Brief of FCC as amicus curiae at 27–28.

The only reasons given for the FCC request is that, by adding the proviso, the Court would avoid misunderstandings, and that to do so would comply with the Supreme Court's expressed preference for conditional decrees.

The addition of a clause which, by the Commission's own concession, would have no effect either on the authority of the Commission or that of the Court, is more likely to create misunderstandings than to eliminate them. As for the alternate argument, the Court does not view the requirement of a proviso in a case decided sixty years ago under totally different circumstances to constitute an adequate reason for adding a similar clause here.

The Court has recognized and discussed the jurisdiction of the FCC ever since its opinion of September 11, 1978. *United States* v. *AT&T*, *supra*, 461 F. Supp. 1314. As the Court

then decided, and subsequently reiterated,[338] none of the activities of AT&T which is the subject of these lawsuits is immunized from the antitrust laws by virtue of FCC regulation. The Court has also noted that there is no reason to anticipate a conflict between the decree and federal regulation, but that if such a conflict arose, it appeared likely that, in view of the Commission's limited authority in regard to structural matters in the telecommunications industry, the judgment of an antitrust court would prevail. *Cf.* Part III *supra*. Indeed, the FCC itself has conceded herein that it has limited authority with respect to the structure of the telephone industry. Memorandum of the FCC as amicus curiae in *United States* v. *AT&T*, reprinted at 62 F.C.C.2d 1102, 1117-18 (1977). For these reasons, a modification of the proposed decree along the lines requested by the FCC is unnecessary.

E. Cincinnati Bell

The Ohio Office of the Consumers' Counsel and the City of Cincinnati, object to Section I(A)(3) of the proposed decree which requires termination of the license contracts, including the one with Cincinnati Bell.[339] These entities argue that in 1903, AT&T made an agreement[340] with Cincinnati Bell pursuant to which AT&T received approximately 29 percent of Cincinnati Bell's common stock[341] in exchange for a com-

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[338] See *United States* v. *AT&T*, 524 F. Supp. at 1357-60.

[339] Cincinnati Bell is covered by the proposed decree notwithstanding the fact that it is not one of the twenty-two Operating Companies to be divested because Section I(A)(3) of the proposed decree calls for "the termination of the License Contracts between AT&T and the BOCs and other subsidiaries." Section IV of the proposed decree, in turn, defines subsidiary as "any organization or entity in which AT&T has stock ownership, whether or not controlled by AT&T." Thus, these provisions include Cincinnati Bell as well as the Southern New England Telephone Company.

[340] The minutes of a Board of Directors meeting are alleged to substantiate their claim.

[341] There is some question whether the stock was worth $70 million or about one-half that amount.

mitment by AT&T to provide Cincinnati Bell with the benefits of the license contracts in perpetuity. The proposed termination of all license contracts, including the one pertaining to Cincinnati Bell, is claimed to constitute a confiscation of the stock and a windfall to AT&T.

The Justice Department responds that negotiations between AT&T and Cincinnati Bell are under way to resolve this issue (Response to Comments at 38, n. *) and AT&T states that the license contracts will be terminated "on a reasonable and equitable basis," but that if Cincinnati Bell is dissatisfied with the outcome, it may bring a separate action and assert whatever contract remedies it may have. AT&T Reply Brief at 120, n. *.

The Court regards these responses as adequate, particularly because Cincinnati Bell itself has not complained of the termination of the license contracts or indicated that it expects the current negotiations to prove unsatisfactory. It may well be that the issue will, in fact, be resolved amicably between Cincinnati Bell and AT&T. If, after the plan of reorganization is submitted, Cincinnati Bell is dissatisfied with the terms of the termination, it may raise the issue,[342] and the Court will then determine whether the matter is appropriately addressed in the context of the reorganization or by way of a separate legal action.

## XI
## Future Proceedings

The Court has received a number of comments urging it to hold a variety of future proceedings in connection with the implementation of the proposed decree. Some go so far as to suggest that the Court withhold its approval of the decree until the contents of the reorganization plan are known; others argue more simply that the decree be modified to include mechanisms for Court and third-party involvement in both the implementation and the enforcement of the decree; still others contend that the Operating Companies be immediately

[342] See Part XI *infra*.

drawn into the public interest process on an independent basis. Each of these issues is discussed below.

A. Deferral of Approval of the Judgment

It has been widely contended that the Court should defer either approving or disapproving the parties' proposal, or that, at a minimum, it should grant only tentative approval until it has had an opportunity to review AT&T's plan of reorganization. Implicit in these suggestions is the premise that it is not possible now to determine whether the broad principles set forth in the proposed decree, even if fully implemented, comply with the Tunney Act's public interest standard, and that a *de novo* public interest evaluation must therefore be conducted after the plan of reorganization has been submitted.

There is no sound basis for such a course. Although, as discussed above, many important questions are left unresolved, the proposal does set forth the principles of the parties' agreement with sufficient particularity that the Court is able to make a decision now on the question of whether a judgment based on these principles would be in the public interest Moreover, a deferral of approval or a grant only of tentative approval — essentially on the theory that once implementation begins, entirely new problems of concern to the public in general or to specific interests may emerge — would be unfair to the parties and to the public.

As AT&T correctly points out, "[d]elay holds the most serious consequences for the operation of the network and can only multiply the costs of uncertainty that have plagued the industry far too long."[343] Such a delay would disrupt AT&T's own operations; it would inhibit investment and other business decisions necessary to the maintenance and improvement of the telecommunications network; it would jeopardize the ability of the Bell System's components to raise the outside capital needed for the modernization and expansion of their network; and it would adversely affect the entire

[343] AT&T Reply Comments at 3.

telecommunications industry, and thus indirectly, the nation as a whole.

Because the principles set forth in the decree are specific enough for the Court to make its decision, and because delay, with all its adverse consequences, is unwarranted, the Court will not defer its ruling on whether the proposed decree is in the public interest.

This decision means, of course, that if the parties accept the Court's modifications, the decree as modified will be approved as being in the public interest, and the Court will be unable at some later stage to add new and different provisions.[344] It also follows that the enforcement procedures adopted herein (see *infra*) will be designed only to permit the Court to protect the provisions and principles of the judgment, as entered, against non-compliance and non-enforcement.

B. The Court's Continuing Enforcement Authority

Although the principles underlying the proposed decree are clear, they are in several respects sufficiently general in nature that they could be implemented by the parties in a number of different ways.[345] As to some of these provisions,

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[344] This limitation is without prejudice to the exercise by the Court of authority to modify the judgment stemming not from the decree itself but from general principles of law.

[345] For example, section IV(G)(1) provides that the local exchange areas shall be drawn in such a way as to take account of "common social, economic, and other purposes, even where such configuration transcends municipal or other local governmental boundaries." It is nowhere spelled out what those conditions might be, or how they would be established, defined, or demonstrated. AT&T would thus be wholly free to draw the exchange area boundaries so as to further its own interests at the expense of those of the Operating Companies, at the expense of its various interexchange competitors, or both.

Similarly, section I(A)(1) provides that "sufficient facilities, personnel, systems, and rights to technical information" will be assigned by AT&T to the Operating Companies so as to permit them effectively to perform the functions assigned to them under the judgment. This clause, too, is more precatory than mandatory, more broad than precise, and in particular it

the parties have provided the Court with assurances regarding the approach they will follow.[346] As to others, only their future conduct will reveal whether the principles of the proposed decree are being followed.

The Court's public interest determination necessarily rests on the premise that the parties' assurances will be fully carried out and that the other principles included in the decree will be implemented in the manner most consistent with its purposes. However, no one can know at this time whether this premise is well taken, and it is therefore imperative that the Court retain the power to ensure that the parties comply in full with the principles mandated by the decree, both in formulating the plan of reorganization and in their conduct after divestiture.

The parties provide somewhat differing explanations as to why the Court should be unconcerned about the decree's implementation. AT&T badly states that the Tunney Act authorizes the Court only to approve the decree, not "to assure that it will in fact be implemented."[347] That contention betrays a complete misunderstanding of the purpose of the

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leaves to AT&T wide discretion in the assignment and the configuration of common facilities. As indicated in Part IX, *supra*, the multifunction facilities represent, by the parties' own estimates, about twenty percent of the total Bell System assets — meaning that they have a value of some $20 billion. Unless more definite guidelines are set, there is an obvious and substantial incentive and opportunity for manipulation by AT&T.

[346] Among these principles are the following: (1) AT&T will grant to the Operating Companies on a royalty-free basis all existing patents and all patents to be issued for a period of five years following entry of the judgment; (2) the chief executives of the seven new Operating Companies will have full independence, without interference, from AT&T to provide to the Court their views regarding the plan of reorganization and otherwise; (3) switches providing Class Four functions will be available for the interconnection of AT&T's interexchange competitors if the Operating Companies conclude that this is the most efficient method of effecting the interconnection; (4) the "single point of contact," organized to meet national security and emergency preparedness needs will be sufficiently funded and supported; and (5) the local exchange areas will be drawn in accordance with objective principles and without discrimination.

[347] AT&T Reply Brief at 132, note **.

Act and of the Court's equitable responsibilities. The Congress was concerned with the ever-present possibility of collusion between the Department of Justice and antitrust defendants, with their vast economic and political powers, and for that reason it interposed the Court's public interest authority between the parties and the entry of consent decrees. But that procedure would be largely meaningless if AT&T's understanding of the proper role of the Court were correct. Upon that view, the parties could simply enter into a consent decree which easily passed muster in the public interest proceeding, and then proceed with its implementation, or nonimplementation, without fear of judicial interference. The Court rejects so self-defeating a construction of the law and of its responsibilities.

The Department of Justice's response is more sophisticated but no more satisfactory. The Department states that it will "be fully aware of all aspects of public concern"; that it will "review the plan of reorganization to ensure that [appropriate] arrangements are made"; and that the proposed decree properly "places [sole] responsibility for approval of divestiture in the Department of Justice."[348] In addition, counsel for the government have argued with some vigor that they are committed to this settlement and will do their best to implement and enforce it. The Court does not in the least doubt the good faith of the particular individuals involved. But this is not a matter of personalities — either the Court's or those of specific Justice Department officials[349] The Tunney Act is addressed to institutions: the Congress determined, for reasons it considered good and sufficient, that, on balance, antitrust settlements involving the government shall be sub-

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[348] Department of Justice Brief at 96-99. But the Department has acknowledged that the Court has a legitimate interest in retaining jurisdiction to ensure that the plan of reorganization does not depart from the principles in the judgment. See pp. 159–60 *infra*.

[349] Individuals, of course, come and go. What has remained and is likely to remain constant are AT&T's self-interest and its desire to secure from government officials favorable interpretations of laws, rules, regulations, agreements, and understandings; and the possibility that political or other influence may effectively be brought to bear on public officials.

ject to the scrutiny of the Judiciary. The Court intends to see to it that this mandate is fully implemented in this case.

During the congressional hearings which led to enactment of the statute, the Department of Justice officials argued — just as they do here — that internal Department procedures were adequate to protect the public interest and that judicial involvement was for that reason unnecessary.[350] The Congress rejected that approach in favor of requiring the courts to become active participants in the process.[351] In light of that legislative determination, it would be inappropriate and insufficient for courts to rely exclusively on a Justice Department review as providing an adequate assurance that a consent decree will be implemented in a manner consistent with the public interest.[352]

The procedures requisite for the protection of the public interest necessarily depend upon many different circumstances — which is precisely why the Congress left to the courts' discretion the means by which their public interest responsibilities would be effected. There are several reasons why judicial scrutiny and enforcement beyond the entry of judgment stage is especially necessary in these cases.

First. Whether this decree will, in fact, provide the benefits which underlie the Court's public interest determination depends upon (1) the provisions of the plan of reorganization and (2) the extent to which AT&T and the divested Operating Companies comply with the requirements of the decree

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[350] Senate Hearings, *supra*, note 72, at 90-91, 103-04 (Assistant Attorney General Thomas Kauper); *Consent Decree Bills: Hearings on H.R. 9023, H.R. 9947 and S. 783*, *supra*, note 72 at 62, 71-73, 84-85 (Deputy Assistant Attorney General Bruce Wilson.

[351] See Part II *supra*.

[352] The parties contend that in other cases courts have been content with less than what they have presented here, and that they have not required approval of detailed implementation plans. In fact, consent decrees commonly include clauses requiring judicial approval of plans of reorganization. See, *e.g.*, *United States* v. *American Optical Co.*, 1966 Trade Cas. ¶ 71,781 (E.D. Wis. 1966); *United States* v. *United Fruit Co.*, 1958 Trade Cas. ¶ 68,941 (E.D. La. 1958).

applicable even after the completion of the divestiture.[353] To preclude Court review of these activities would thus be to do precisely that which Congress sought to prevent.

Second. This particular settlement, and this particular consent decree, are of extraordinary magnitude and complexity. The decree will effectuate the largest, most complicated divestiture since the passage of the Tunney Act, if not in all of American legal history. It will not only provide for the reorganization of the largest corporation in the world, but it will also affect the entire telecommunications industry, the computer industry, the dissemination and publication of information, foreign trade, national defense, and thus the interests of literally millions of individuals — ratepayers, AT&T competitors, creditors, employees, stockholders and bondholders, and ordinary American citizens who are dependent upon the telephone for their private or business interests. It would be wholly inappropriate in that kind of situation for the Court to allow the parties to exercise unreviewable discretion over future implementation and enforcement.

Third. The Court has recounted how AT&T and various departments of the government, in particular the Department of Justice and the Department of Defense, have cooperated since the 1950s in a manner that does not instill confidence that their sole motivation and purpose was the protection of the public interest. See Part I *supra*. In view of that history, and in view of the mandate of the Tunney Act, the Court would be derelict in its duties if it relied upon Department of Justice enforcement alone for the protection of the public interest following the signing of the judgment itself.

For all these reasons, it is the Court's conclusion that the purpose of the Tunney Act will be fulfilled only if judicial

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[353] For example, AT&T and its affiliates are required under Section I(C) of the proposed decree to provide research, development, manufacturing, and other support services to the Operating Companies; and pursuant to Appendix B of the proposed decree, the equal exchange access for all interexchange carriers must be provided by September 1, 1986.

scrutiny and enforcement do not cease with the entry of judgment.

It is unclear whether the decree itself vests in the Court the requisite authority *sua sponte* to enforce the judgment, for the parties to the litigation have taken ambiguous and inconsistent positions on this question. By its terms, the proposed decree grants enforcement power only to the parties to the lawsuit (and after divestiture to the Operating Companies), apparently to the exclusion of the Court acting *sua sponte*.[354] The Department's Competitive Impact Statement likewise strongly suggests[355] that only the parties possess such power, and AT&T's briefs are even more emphatic in asserting that "*sua sponte* action by the Court would be unnecessary and unprecedented," and that various commentors are wrong in assuming that "*sua sponte* enforcement action by this Court would be proper." AT&T Brief at 117; AT&T Reply Brief at 133-34.

On the other hand, the Department of Justice has acknowledged elsewhere that, after the judgment has been entered, the "Court will then have the authority to ensure that any actions taken are consistent with the [judgment], and the attendant powers to hold hearings, appoint experts and seek assistance by appropriate means from interested parties." Response to Comments at 15. The Department went on to state that, since the Court would retain jurisdiction pursuant to Section VII of the decree, it would be able on its own motion to initiate proceedings to enforce its provisions,[356] and it further observed that "the Court would retain jurisdiction

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[354] Section VII of the proposed decree provides that

> [j]urisdiction is retained by this Court for the purpose of enabling any of the parties to this Modification of Final Judgment, or, after the reorganization specified in Section I, a BOC to apply to this Court at any time for such further orders or directions as may be necessary or appropriate for the construction or carrying out of this Modification of Final Judgment, for the modification of any of the provisions hereof, for the enforcement of compliance herewith, and for the punishment of any violation hereof.

[355] Competitive Impact Statement at 38.

[356] Department of Justice Response to Comments at 136-37.

to assure that the plan of reorganization ultimately approved by the Department of Justice does not in any substantial way depart from the [judgment's] principles — principles that the Court would have approved and hence mandated."[357]

These confusing and somewhat contradictory interpretations do not provide a firm basis for the Court's action *sua sponte* to initiate enforcement proceedings. If such authority is to be found, it will have to be elsewhere than in the present language of the proposed decree.

Some such authority already exists through the law of contempt. Although civil contempt proceedings may probably[358] be initiated only by a party or parties with an interest in the decree, a court may enforce its own judgments by means of criminal contempt even if there has been no request from a party. *MacNeil* v. *United States*, 236 F.2d 149 (1st Cir. 1956). See also *United States* v. *Barnett*, 346 F.2d 99 (5th Cir. 1965); *United States* v. *International Union*, 190 F.2d 865 (D.C. Cir. 1951); *Fletcher* v. *United States*, 174 F.2d 373 (4th Cir. 1949); *Palmigiano* v. *Garrahy*, 448 F. Supp. 659 (D.R.I. 1978).

There is, however, a glaring defect to the criminal contempt option as a means of enforcing the decree as it is presently drafted: many of the enforcement problems that are likely to arise may be expected to stem from the broad principles set forth in the decree rather than from narrowly-defined, precise provisions. Yet criminal contempt sanctions as a rule may be imposed only for clear-cut violations of very specific judgments or orders. Thus, unless the proposed decree is modified to

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[357] Competitive Impact Statement at 17. To confuse the parties' positions even further, counsel for the Department suggested during oral argument that under the decree the Court could act on its own motion, but only in the event that the Department had failed in bad faith to undertake its own enforcement efforts. Hearing on June 30, 1982, Tr. 25445-47.

[358] It may be that, in a case of this kind, where the Court has in effect placed its imprimatur on the decree by virtue of a comprehensive public interest proceeding, it would be a party in interest with sufficient standing for civil contempt purposes. It is not necessary to come to a definite conclusion on this matter at this time.

allow for the entry of such orders in implementation of the decree's principles, the Court would probably be left without any realistic means of redressing the difficulties that are likely to arise in the implementation phase of the judgment. For the reasons stated, this would not be in the public interest.

The Court will accordingly require as a condition of its approval of the proposed decree that it be modified (1) to require Court approval of the plan of reorganization and (2) to confirm the Court's authority to initiate enforcement proceedings *sua sponte*. These modifications will enable the Court both directly to enforce specific provisions of the decree and to issue orders construing its principles in more specific terms so that, if there is a violation, sufficient grounds will exist for the entry of further enforcement orders or the imposition of appropriate punishment.

C. Status of Third Parties

A number of individuals as well as several governmental and private entities have sought to intervene in these proceedings.[359] Although the Court rejected all these requests at the time they were made, it did, in its order of May 25, 1982, invite interested parties to advise it of the status they sought with respect to further proceedings.[360] In response to that invitation, a number of interested persons and organizations replied that they wished to be granted status as intervenors, and they generally suggested that this should

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[359] See notes 60-61 *supra*.

[360] Specifically, the Court's memorandum stated that

> Interested persons shall indicate (1) whether they request participation as intervenors, amicus curiae, or in some other capacity; (2) whether such status would be limited to certain topics or phases of the proceedings; (3) what specific powers they would expect to be able to exercise (*e.g.*, present evidence, file procedural motions or counterclaims, take appeals, acquire the right to veto the settlement); and (4) why such status and such powers are necessary for the safeguarding of their legitimate interests and appropriate in the circumstances of this case [citing a previous Court memorandum].

Order filed May 25, 1982, at 5.

include the right to present evidence, to call and cross-examine witnesses, to file procedural motions and counterclaims, and to take appeals.[361]

It is clear from the language of the Tunney Act, its legislative history, and from the cases[362] that there is no right to intervene; to the contrary, Congress intended intervention, and the scope of the intervention if allowed, to be discretionary.

The Tunney Act provides that in making its public interest determination, "the court *may* . . . authorize full or limited participation in proceedings before the court by interested persons or agencies, including . . . intervention as a party pursuant to the Federal Rules of Civil Procedure." 15 U.S.C. § 16(f) (emphasis added). Nothing in the legislative history of the Act or in any decision construing it lends support for

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[361] No one asserted a sufficient reason for receiving a right to veto the settlement. There was little response to the Court's inquiry as to the need for intervention or its appropriateness in the circumstances of these cases.

[362] There are no court decisions holding that the Tunney Act grants a right to intervene. Decisional law prior to passage of the Act is generally to the same effect. One exception is *Cascade Natural Gas Corp.* v. *El Paso Natural Gas Co.*, 386 U.S. 129 (1967), but it involved a unique fact situation. The Supreme Court had ordered divestiture as part of its decision on the merits but no action had been taken to carry out the mandate. Instead, the parties filed a consent decree which did "the opposite of what [the Court's] prior opinion and mandate commanded." *Id.* at 142. In that posture, the Court found a right to intervene. The cases are virtually unanimous in limiting the *Cascade* decision to its peculiar facts. For example when a third party sought to intervene in the *Western Electric* case, the court denied the application, finding *Cascade* to be limited to its "extraordinary circumstances," and that decision was affirmed by the Supreme Court. *United States* v. *Western Electric Co.*, 1968 Trade Cas. § 72, 415 (D.N.J.), *aff'd*, 392 U.S. 659 (1968). See also *United States* v. *Associated Milk Producers, Inc.*, 534 F.2d 113 (8th Cir. 1976); *Smuck* v. *Hobson*, 408 F.2d 175, 179 n. 16 (D.C. Cir. 1969); *United States* v. *Carrols Development Corp.*, 454 F. Supp. 1215, 1220-21 (N.D.N.Y. 1978); *United States* v. *Paramount Pictures, Inc.*, 333 F. Supp. 1100, 1102 (S.D.N.Y.), *aff'd*, 404 U.S. 802 (1971); *United States* v. *Automobile Manufacturers Ass'n*, 307 F. Supp. 617, 619 (C.D. Cal. 1969), *aff'd*, 397 U.S. 248 (1970); *United States* v. *Blue Chip Stamp Co.*, 272 F. Supp. 432 (C.D. Cal. 1967), *aff'd*, 389 U.S. 580 (1968).

the proposition that the Congress intended "may" to mean "shall." In the congressional reports and hearings, it was repeatedly emphasized that the court conducting a Tunney Act proceeding would have the widest possible latitude in choosing the appropriate method for collecting the information necessary to make its decision and that the various means specified in the subsection were to be regarded as permissive.[363]

The applicants for intervention have already been accorded substantial rights in these proceedings — rights which for all intents and purposes have been equal to those possessed with respect to the public interest proceeding by the parties to these lawsuits. In addition to their voluminous comments, they have been permitted to file briefs and reply briefs and through lead counsel they have participated in oral argument. The Court has considered their several procedural and substantive arguments, requests, and recommendations, and a fair number of them have resulted in favorable action. The question now is what participation, if any, should be permitted with respect to future proceedings.

As the substantive portions of this opinion show, the Court has concluded that none of the issues before it requires an evidentiary hearing. That being so, there is obviously no need, nor indeed any occasion, for the presentation by a third party of its own witnesses or for the cross-examination of adverse witnesses. As for the filing of motions or counterclaims, the Court has not been advised of the substance of such pleadings or of the claims or issues to which they might be addressed. More importantly, there will be no occasion for the filing of motions and counterclaims prior to the entry of the judgment for, if the government and AT&T agree to the modifications required by the Court, no further proceedings will be held prior to the entry of judgment.[364]

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[363] See, *e.g.*, S. Rep. No. 93-298, *supra*, at 6 (broad discretion); *Senate Hearings*, *supra*, note 72 at 453 (procedural devices are discretionary in nature) (Sen. Tunney); *Id.* at 149, 152 (necessary information to be adduced through simplest and least time-consuming means) (Judge J. Skelly Wright).

[364] Intervenor status would not be appropraite simply in the abstract.

The situation is different, however, regarding post-judgment proceedings.[365] The Court intends to conduct proceedings prior to its approval of AT&T's plan of reorganization that will be procedurally similar to the proceedings which the Tunney Act requires in advance of the entry of judgment.[366] The Court expects that interested persons and organizations will be given an opportunity to file comments or briefs; there may be oral argument; and, should it appear that factual development would be helpful, there may be evidentiary hearings at which appropriate third parties will be permitted to participate with full rights. These purposes can best be achieved by granting intervenor status to all those who have filed requests or motions to intervene.

At the time the decree is entered, the Court will issue an order describing the rights of intervenors.[367] These will include: (1) the right to appeal the entry of the decree; (2) full participation in the proceedings which the Court will conduct to determine whether to approve the plan of reorganization; and (3) the right to appeal from the Court's decision concerning the plan of reorganization. Intervenor status will terminate thereafter.

Several third parties have requested the grant of authority, either by way of intervenor status or otherwise, to enforce the judgment after the plan of reorganization has been submitted and approved. These requests pose a difficult problem. On the one hand, it is entirely appropriate, for the reasons discussed above, that the judgment continue to be

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As indicted *supra*, the Tunney Act does not require the full formalities extant in normal litigation unless they are needed for the development of information useful to the public interest determination.

[366] In order to permit interested persons to challenge the Court's public interest determination, they will be allowed to intervene for the purpose of appealing the entry of the decree.

[367] Substantively, the proceeding will be limited to an examination of plan's consistency with the judgment. See Subpart A *supra*.

[368] There is no doubt that the Court may authorize intervention on a limited basis. The Tunney Act itself allows the Court to provide for "full or limited participation." 15 U.S.C. § 16(f)(3).

enforced, if necessary by the Court, past the time when the plan of reorganization is approved. The actual divestiture will not occur for eighteen months after formal approval of the plan. Moreover, even after the divestiture significant actions will need to be taken in implementation of the judgment.[368] On the other hand, means must be found for avoiding constant, unnecessary interference by AT&T's competitors and others with implementation of the reorganization and with the normal operations of AT&T and the divested Operating Companies. Furthermore, once the judgment has been entered and the plan of reorganization has been approved, this Court should not be burdened with innumerable requests for clarification, modification, and charges of violation.[369]

To strike an appropriate balance, the Court has decided upon a procedure for the participation of third parties after approval of the reorganization plan which combines the process adopted in *United States* v. *Associated Milk Producers, Inc.*, 394 F. Supp. 29, 46 (W.D. Mo. 1975), *aff'd*, 534 F.2d 113 (8th Cir. 1976) with the government's "bad faith" proposal made in a different context. See note 357 *supra*.

In the *Milk Producers* case, the court, after a finding that a proposed decree was in the public interest, issued an order providing that any interested person who believed that "defendant is not complying with the terms of the Final Judgment," would be authorized to serve upon the Department of Justice a request for enforcement. If the Department refused to bring an enforcement action in response to the request, both that request and the Department's response were to be submitted to the court for a determination of "what, if any, further appropriate proceedings should be directed." This procedure appears to have worked well.[370]

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[368] See note 353 *supra*.

[369] In view of the large number and the variety of interested parties, that contingency is very real.

[370] See *United States* v. *Associated Milk Producers, Inc.*, 477 F. Supp. 671 (W.D. Mo. 1979).

In the exercise of its authority under the Tunney Act, its general equitable powers, and pursuant to Rule 24, Fed. R. Civ. P., the Court will, after the decree has been entered, issue an order which will establish a similar complaint and response procedure, with the proviso, however, that application to the Court may be made only after application for enforcement is first made to the Department of Justice. The application to the Court must be accompanied by an affidavit alleging facts with particularity[371] which, if true, would demonstrate a bad faith refusal by the Department of Justice to enforce the judgment.[372] As in the *Milk Producers* case, the Court will decide upon receipt of such documents what, if any, further proceedings should be initiated.

D. Participation of the Bell Operating Companies

Many persons and organizations have questioned the lack of independent representation for the Operating Companies in this proceeding, both prior to the entry of judgment and in conjunction with the preparation of the plan of reorganization. They contend that AT&T's interests under the proposed settlement are diametrically opposed to those of the Operating Companies, and that AT&T therefore cannot be relied upon to act in the Operating Companies' best interests. They suggest that, for these reasons, the Court should ensure the proper representation of the Operating Companies either by divesting them immediately or by appointing a guardian *ad litem* or similar officer to represent their interests. Such participation will not be ordered at this stage of the proceedings, both because it is not necessary, and, more fundamentally, because there is no practical means for effecting it.

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[371] Cf. Rule 9(b), Fed. R. Civ. P.

[372] Some third parties might, of course, independently have standing to enforce the decree apart from this specific procedure for their participation. See *Natural Resources Defence Council* v. *Costle*, 561 F.2d 904 (D.C. Cir. 1977); Sullivan, *Enforcement of Government Antitrust Decrees by Private Parties: Third Party Beneficiary Rights and Intervenor Status*, 123 U. Pa. L. Rev. 822 (1975); Berger and Bernstein, *An Analytical Framework for Antitrust Standing*, 86 Yale L. J. 809 (1977).

First. It is not at all clear that AT&T will act contrary to the interests of the Operating Companies. Under the proposed decree, AT&T's shareholders will become the shareholders of the Operating Companies and, should AT&T act to undermine the interests of these Companies or fail appropriately to protect them, it and its managers might be liable civilly for breach of their fiduciary duty to these shareholders. See Part IX *supra*. Moreover, since the divested Operating Companies will supply AT&T's sole avenue of access to telephone subscribers and will potentially be large purchasers of Western Electric equipment, AT&T has additional incentives to protect their interests.

Second. The views which the Operating Companies might be expected to espouse have substantially been presented in this proceeding. With respect to all of the issues which presumably would concern the Operating Companies — principally the distribution of the assets and the corporate debt, the restrictions on Operating Company operations, the Operating Company access requirements — able parties with able counsel have presented to the Court the factual, legal, and policy arguments bearing upon these questions. In the main, the Operating Companies would have no particular expertise that would give special value to their participation: the Court's decision generally rests upon the rationale of improved competition, and the relevant information on that subject is available to those who are now before the Court. That is not to say, certainly, that the Operating Companies, if they had independent representation, would not make a contribution; obviously they could and would. But in the opinion of the Court that contribution is not so critical as to outweigh the adverse factors recited below.

Third. There is no existing procedural mechanism which would lend itself to the expression of the veiws of the Operating Companies. Two alternatives have been advanced: an immediate spin-off of the Operating Companies so as to enable them to bargain with AT&T and the Justice Department concerning the terms of the proposed decree, and the appointment of a guardian or trustee to represent their interests in this and future proceedings.

An immediate spin-off of the Operating Companies, while superficially appealing, would be entirely impractical and, notwithstanding the Court's urging, none of those who has advocated such a spin-off has presented a plan that is even remotely feasible. In fact, such an action would leave entirely unresolved all of the problems of administrative coordination, interconnection, and continuity of service that are addressed in the proposed decree.

For example, as a consequence of such a spin-off, the Operating Companies would be wholly independent of AT&T, providing to AT&T neither services nor assistance. At a minimum, this would leave AT&T at a serious disadvantage relative to competitors who have constructed their own complete networks among major cities;[373] at worst, this course would disrupt, for months or perhaps years, the nation's telecommunications network, with incalculable consequences to trade and defense, as well as to ordinary communication and interaction among citizens. At the same time, such a spin-off would leave local and interexchange facilities integrated under the common ownership of the Operating Companies, and it would thus be directly contrary to the antitrust objectives of these lawsuits. The Court will not attempt to catalogue all of the other problems and difficulties that would inevitably accompany a separation without advance planning or agreement similar to that embodied in the proposed decree; but there can be no question but that, in a separation of this magnitude, they would be manifold and in all likelihood insurmountable.[374] As indicated, beyond expressing the general expectation that all those matters may somehow be

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[373] The Operating Companies own most of the facilities necessary for the provision of interexchange service. See Exhibit D-24B-1011. The functioning of AT&T's Long Lines Department would be substantially impaired if the Operating Companies were divested intact.

[374] Much of the impetus for an immediate spin-off results from the belief that there should be arm's length bargaining regarding the valuation of the assets being divided between AT&T and the Operating Companies. That argument in favor of an immediate spin-off is meritless, however, because the Court has concluded that net book value rather than market value is the appropriate standard for this division. See Part IX *supra*.

worked out, not one person or organization has even attempted to suggest practical solutions. For all these reasons, then, the Court has concluded that it will not require an immediate spin-off.

While the Court's power to appoint a guardian, trustee, or similar officer to represent the interests of the Operating Companies is far from clear, its rejection, again, must be bottomed primarily upon the practical difficulties inherent in this approach. If a guardian were appointed at this time, even before the plan of reorganization has been formulated, he could be expected to face considerable difficulty in obtaining the type of detailed information from the Operating Companies which would be the *raison d'etre* of his participation. The personnel of the Operating Companies and the information they possess would remain under the control of AT&T and it is unlikely that a guardian could secure sufficient assistance from them at this stage to warrant the disruption his appointment would entail. Development of an independent expertise by the guardian would be likely to take years, further delaying resolution of this litigation without the promise of any real benefits to the decision-making process.

Participation by the Operating Companies, through their own chief executive officers, will be appropriate, however, with respect to the process of implementation of the decree. At the time the plan of reorganization is presented, the seven new regional Operating Companies and their chief executives will be a long way on the road toward independence, with a substantial incentive to represent and advocate their own interests. Moreover, their familiarity with the facilities required to provide local and intercity service and exchange access would give them special expertise concerning the adequacy of the reorganization plan in regard to the division of assets.

The Court accordingly intends to require that, at the time the plan of reorganization is submitted to the Court by the Department of Justice, the designated chief executive officers of the seven regional Operating Companies file with the Court sworn statements certifying that, to the best of their knowl-

edge, the plan will leave the companies which they head as viable entities with the resources necessary to perform the functions described in the decree. These statements will also be expected to discuss any element of the plan of reorganization that may have been imposed by AT&T over the objections of any chief executive officer.[375] The Court expects, additionally, to call upon the chief executive officers or their staffs to participate in other respects as well in the proceedings held at the time the plan of reorganization is presented for judicial approval.

## XII
## CONCLUSION

The proposed reorganization of the Bell System raises issues of vast complexity. Because of their importance, not only to the parties but also to the telecommunications industry and to the public, the Court has discussed the various problems in substantial detail. It is appropriate to summarize briefly the major issues and the Court's decisions which are central to the proceeding.

A. The American telecommunications industry is presently dominated by one company — AT&T. It provides local and long-distance telephone service; it manufactures and markets the equipment used by telephone subscribers as well as that used in the telecommunications network; and it controls one of the leading communications research and development facilities in the world. According to credible evidence, this integrated structure has enabled AT&T for many years to undermine the efforts of competitors seeking to enter the telecommunications market.

The key to the Bell System's power to impede competition has been its control of local telephone service. The local

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[375] In order to enable the Court to assess the weight to be accorded to the statements of these individuals, they will also be invited, but not required, to reveal any continuing relationship they may have with AT&T (*i.e.*, reemployment rights, pension plans, informal promises of executive position with AT&T).

telephone network functions as the gateway to individual telephone subscribers. It must be used by long-distance carriers seeking to connect one caller to another. Customers will only purchase equipment which can readily be connected to the local network through the telephone outlets in their homes and offices. The enormous cost of the wires, cables, switches, and other transmission facilities which comprise that network has completely insulated it from competition. Thus, access to AT&T's local network is crucial if long distance carriers and equipment manufacturers are to be viable competitors.

AT&T has allegedly used its control of this local monopoly to disadvantage these competitors in two principal ways. First, it has attempted to prevent competing long distance carriers and competing equipment manufacturers from gaining access to the local network, or to delay that access, thus placing them in an inferior position vis-a-vis AT&T's own services. Second, it has supposedly used profits earned from the monopoly local telephone operations to subsidize its long distance and equipment businesses in which it was competing with others.

For a great many years, the Federal Communications Commission has struggled, largely without success, to stop practices of this type through the regulatory tools at its command. A lawsuit the Department of Justice brought in 1949 to curb similar practices ended in an ineffectual consent decree. Some other remedy is plainly required; hence the diversiture of the local Operating Companies from the Bell System. This divestiture will sever the relationship between this local monopoly and the other, competitive segments of AT&T, and it will thus ensure — certainly better than could any other type of relief — that the practices which allegedly have lain heavy on the telecommunications industry will not recur.

B. With the loss of control over the local network, AT&T will be unable to disadvantage its competitors, and the restrictions imposed on AT&T after the government's first antitrust suit — which limited AT&T to the provision of

telecommunications services — will no longer be necessary. The proposed decree accordingly removes these restrictions.

The decree will thus allow AT&T to become a vigorous competitor in the growing computer, computer-related, and information markets. Other large and experienced firms are presently operating in these markets, and there is therefore no reason to believe that AT&T will be able to achieve monopoly dominance in these industries as it did in telecommunications. At the same time, by use of its formidable scientific, engineering, and management resources, including particularly the capabilities of Bell Laboratories, AT&T should be able to make significant contributions to these fields, which are at the forefront of innovation and technology, to the benefit of American consumers, national defense, and the position of American industry vis-a-vis foreign competition.

All of these developments are plainly in the public interest, and the Court will therefore approve this aspect of the proposed decree, with one exception. Electronic publishing, which is still in its infancy, holds promise to become an important provider of information — such as news, entertainment, and advertising — in competition with the traditional print, television, and radio media; indeed, it has the potential, in time, for actually replacing some of these methods of disseminating information.

Traditionally, the Bell System has simply distributed information provided by others; it has not been involved in the business of generating its own information. The proposed decree would, for the first time, allow AT&T to do both, and it would do so at a time when the electronic publishing industry is still in a fragile state of experimentation and growth and when electronic information can still most efficiently and most economically be distributed over AT&T's long distance network. If, under these circumstances, AT&T were permitted to engage both in the transmission and the generation of information, there would be a substantial risk not only that it would stifle the efforts of other electronic publishers but that it would acquire a substantial monopoly over the generation of news in the more general sense. Such

a development would strike at a principle which lies at the heart of the First Amendment: that the American people are entitled to a diversity of sources of information. In order to prevent this from occurring, the Court will require, as a condition of its approval of the proposed decree, that it be modified to preclude AT&T from entering the field of electronic publishing until the risk of its domination of that field had abated.

C. After the divestiture, the Operating Companies will possess a monopoly over local telephone service. According to the Department of Justice, the Operating Companies must be barred from entering all competitive markets to ensure that they will not misuse their monopoly power. The Court will not impose restrictions simply for the sake of theoretical consistency. Restrictions must be based on an assessment of the realistic circumstances of the relevant markets, including the Operating Companies' ability to engage in anticompetitive behavior, their potential contribution to the market as an added competitor for AT&T, as well as upon the effects of the restrictions on the rates for local telephone service.

This standard requires that the Operating Companies be prohibited from providing long distance services and information services, and from manufacturing equipment used in the telecommunications industry. Participation in these fields carries with it a substantial risk that the Operating Companies will use the same anticompetitive techniques used by AT&T in order to thwart the growth of their own competitors. Moreover, contrary to the assumptions made by some, Operating Company involvement in these areas could not legitimately generate subsidies for local rates. Such involvement could produce substantial profits only if the local companies used their monopoly position to dislodge competitors or to provide subsidy for their competitive services or products — the very behavior the decree seeks to prevent.

Different considerations apply, however, to the marketing of customer premises equipment — the telephone and other devices used in subscribers' homes and offices — and the production of the Yellow Pages advertising directories. For

a variety of reasons, there is little likelihood that these companies will be able to use their monopoly position to disadvantage competitors in these areas. In addition, their marketing of equipment will provide needed competition for AT&T, and the elimination of the restriction on their production of the Yellow Pages will generate a substantial subsidy for local telephone rates.[376] The Court will therefore require that the proposed decree be modified to remove the restrictions on these two types of activities.

D. With respect to a number of subjects, the proposed decree establishes merely general principles and objectives, leaving the specific implementing details for subsequent action, principally by the plan of reorganization which AT&T is required to file within six months after entry of the judgment. The parties have also made informal promises, either to each other or to the Court, as to how they intend to interpret or implement various provisions. The Court has decided that its public interest responsibilities require that it establish a process for determining whether the plan of reorganization and other, subsequent actions by AT&T actually implement these principles and promises in keeping with the objectives of the judgment. Absent such a process, AT&T would have the opportunity to interpret and implement the broad principles of the decree in such a manner as to disadvantage it competitors, the Operating Companies, or both, or otherwise to act in a manner contrary to the public interest as interpreted by the Court in this opinion.

For that reason, the Court is requiring that the judgment be modified (1) to vest authority in the Court to enforce the provisions and principles of that judgment on its own rather than only at the request of a party; and (2) to provide for a

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[376] The decree also provides for another method of subsidizing these rates. It permits the Operating Companies, under the supervision of state and federal regulators, to levy access charges upon long distance carriers and those companies that provide information services. These charges may, if the regulators desire, be set at levels which continue the present level of subsidy for local telephone rates.

proceeding, accessible to third party intervenors and to the chief executives of the seven new regional Operating Companies, in which the Court will determine whether the plan of reorganization is consistent with the decree's general principles and promises.

E. For the reasons stated in this opinion, the Court will approve the proposed decree as in the public interest provided that the parties agree to the addition of the following new section:

## VIII
### MODIFICATIONS

A. Notwithstanding the provisions of section II(D)(2), the separated BOCs shall be permitted to provide, but not manufacture, customer premises equipment.

B. Notwithstanding the provisions of section II(D)(3), the separated BOCs shall be permitted to produce, publish, and distribute printed directories which contain advertisements and which list general product and business categories, the service or product providers under these categories, and their names, telephone numbers, and addresses.

Notwithstanding the provisions of sections I(A)(1), I(A)(2), I(A)(4), all facilities, personnel, systems, and rights to technical information owned by AT&T, its affiliates, or the BOCs which are necessary for the production, publication, and distribution of printed advertising directories shall be transferred to the separated BOCs.

C. The restrictions imposed upon the separated BOCs by virtue of section II(D) shall be removed upon a showing by the petitioning BOC that there is no substantial possibility that it could use its monopoly power to impede competition in the market it seeks to enter.

D. AT&T shall not engage in electronic publishing over its own transmission facilities. "Electronic publishing" means the provision of any information which AT&T or its affiliates has, or has caused to be, originated, authored, compiled, collected, or edited, or in which it

has a direct or indirect financial or proprietary interest, and which is disseminated to an unaffiliated person through some electronic means.

Nothing in this provision precludes AT&T from offering electronic directory services that list general product and business categories, the service or product providers under these categories, and their names, telephone numbers, and addresses; or from providing the time, weather, and such other audio services as are being offered as of the date of the entry of the decree to the geographic areas of the country receiving those services as of that date.

Upon application of AT&T, this restriction shall be removed after seven years from the date of entry of the decree, unless the Court finds that competitive conditions clearly require its extension.

E. If a separated BOC provides billing services to AT&T pursuant to Appendix B(C)(2), it shall include upon the portion of the bill devoted to interexchange services the following legend:

> This portion of your bill is provided as a service to AT&T. There is no connection between this company and AT&T. You may choose another company for your long distance telephone calls while still receiving your local telephone service from this company.

F. Notwithstanding the provisions of Appendix B(C)(3), whenever, as permitted by the decree, a separated BOC fails to offer exchange access to an interexchange carrier that is equal in type and quality to that provided for the interexchange traffic of AT&T, the tariffs filed for such less-than-equal access shall reflect the lesser cost, if any, of such access as compared to the exchange access provided AT&T.

G. Facilities and other assets which serve both AT&T and one or more BOCs shall be transferred to the separated BOCs if the use made by such BOC or BOCs predominates over that of AT&T. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

H. At the time of the transfer of ownership provided for in section I(A)(4), the separated BOCs shall have

debt ratios of approximately forty-five percent (except for Pacific Telephone and Telegraph Company which shall have a debt ratio of approximately fifty percent), and the quality of the debt shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

I. The Court may not act *sua sponte* to issue orders or directions for the construction or carrying out of this decree, for the enforcement of compliance therewith, and for the punishment of any violation thereof.

J. Notwithstanding the provisions of section I(A), the plan of reorganization shall not be implemented until approved by the Court as being consistent with the provisions and principles of the decree.

F. The United States and AT&T shall within fifteen days hereof submit to the Court their proposed decree, including the modifications listed above, or their statements that they are not prepared to incorporate such modifications. If a modified decree is submitted, the Court will promptly approve it as being in the public interest, and the *AT&T* action will be dismissed. If the parties do not agree to incorporate the modifications, the Court will decline to approve the proposed decree, the 1956 consent decree in the *Western Electric* action will remain in effect, and the *AT&T* trial will resume at a date to be set by the Court.

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Harold H. Greene
United States District Judge

Dated: August 11, 1982.

S/_____

MODIFICATION OF FINAL JUDGMENT

(Entered August 24, 1982)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INCORPORATED, AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |

MODIFICATION OF FINAL JUDGMENT

Plaintiff, United States of America, having filed its complaint herein on January 14, 1949; the defendants having appeared and filed their answer to such complaint denying the substantive allegations thereof; the parties, by their attorneys, having severally consented to a Final Judgment which was entered by the Court on January 24, 1956, and the parties having subsequently agreed that modification of such Final Judgment is required by the technological, economic and regulatory changes which have occurred since the entry of such Final Judgment;

Upon joint motion of the parties and after hearing by the Court, it is hereby

ORDERED, ADJUDGED, AND DECREED that the Final Judgment entered on January 24, 1956, is hereby vacated in its entirety and replaced by the following items and provisions:

## I

## AT&T Reorganization

A. Not later than six months after the effective date of this Modification of Final Judgment, defendant AT&T shall submit to the Department of Justice for its approval, and thereafter implement, a plan of reorganization. Such plan shall provide for the completion, within 18 months after the effective date of this Modification of Final Judgment, of the following steps:

1. The transfer from AT&T and its affiliates to the BOCs, or to a new entity subsequently to be separated from AT&T and to be owned by the BOCs, of sufficient facilities, personnel, systems, and rights to technical information to permit the BOCs to perform, independently of AT&T, exchange telecommunications and exchange access functions, including the procurement for, and engineering, marketing and management of, those functions, and sufficient to enable the BOCs to meet the equal exchange access requirements of Appendix B;

2. The separation within the BOCs of all facilities, personnel and books of account between those relating to the exchange telecommunications or exchange access functions and those relating to other functions (including the provision of interexchange switching and transmission and the provision of customer premises equipment to the public); provided that there shall be no joint ownership of facilities, but appropriate provision may be made for sharing, through leasing or otherwise, of multifunction facilities so long as the separated portion of each BOC is ensured control over the exchange telecommunications and exchange access functions;

3. The termination of the License Contracts between AT&T and the BOCs and other subsidiaries and the Standard Supply Contract between Western Electric and the BOCs and other subsidiaries; and

4. The transfer of ownership of the separated portions of the BOCs providing local exchange and exchange access services from AT&T by means of a spin-off of stock of the separated BOCs to the shareholders of AT&T, or by other

disposition; provided that nothing in this Modification of Final Judgment shall require or prohibit the consolidation of the ownership of the BOCs into any particular number of entities.

B. Notwithstanding separation of ownership, the BOCs may support and share the costs of a centralized organization for the provision of engineering, administrative and other services which can most efficiently be provided on a centralized basis. The BOCs shall provide, through a centralized organization, a single point of contact for coordination of BOCs to meet the requirements of national security and emergency preparedness.

C. Until September 1, 1987, AT&T, Western Electric, and the Bell Telephone Laboratories, shall, upon order of any BOC, provide on a priority basis all research, development, manufacturing, and other support services to enable the BOCs to fulfill the requirements of this Modification of Final Judgment. AT&T and its affiliates shall take no action that interferes with the BOCs' requirements of nondiscrimination established by section II.

D. After the reorganization specified in paragraph I(A)(4), AT&T shall not acquire the stock or assets of any BOC.

## II
## BOC Requirements

A. Subject to Appendix B, each BOC shall provide to all interexchange carriers and information service providers exchange access, information access, and exchange services for such access on an unbundled, tariffed basis, that is equal in type, quality, and price to that provided to AT&T and its affiliates.

B. No BOC shall discriminate between AT&T and its affiliates and their products and services and other persons and their products and services in the:

1. procurement of products and services;

2. establishment and dissemination of technical information and procurement and interconnection standards;

3. interconnection and use of the BOC's telecommunications service and facilities or in the charges for each element of service; and

4. provision of new services and the planning for and implementation of the construction or modification of facilities, used to provide exchange access and information access.

C. Within six months after the reorganization specified in paragraph I(A)(4), each BOC shall submit to the Department of Justice procedures for ensuring compliance with the requirements of paragraph B.

D. After completion of the reorganization specified in section I, no BOC shall, directly or through any affiliated enterprise:

1. provide interexchange telecommunications services or information services;

2. manufacture or provide telecommunications products or customer premises equipment (except for provision of customer premises equipment for emergency services); or

3. provide any other product or service, except exchange telecommunications and exchange access service, that is not a natural monopoly service actually regulated by tariff.

## III

## Applicability and Effect

The provisions of this Modification of Final Judgment, applicable to each defendant and each BOC, shall be binding upon said defendants and BOCs, their affiliates, successors and assigns, officers, agents, servants, employees, and attorneys, and upon those persons in active concert or participation with each defendant and BOC who receive actual notice of this Modification of Final Judgment by personal service or otherwise. Each defendant and each person bound by the prior sentence shall cooperate in ensuring that the provisions of this Modification of Final Judgment are carried out. Neither this Modification of Final Judgment nor any of its terms or provisions shall constitute any evidence against, an admission

by, or an estoppel against any party or BOC. The effective date of this Modification of Final Judgment shall be the date upon which it is entered.

## IV
## DEFINITIONS

For the purposes of this Modification of Final Judgment:

A. "Affiliate" means any organization or entity, including defendant Western Electric Company, Incorporated, and Bell Telephone Laboratories, Incorporated, that is under direct or indirect common ownership with or control by AT&T or is owned or controlled by another affiliate. For the purposes of this paragraph, the terms "ownership" and "owned" mean a direct or indirect equity interest (or the equivalent thereof) of more than fifty (50) percent of an entity. "Subsidiary" means any organization or entity in which AT&T has stock ownership, whether or not controlled by AT&T.

B. "AT&T" shall mean defendant American Telephone and Telegraph Company and its affiliates.

C. "Bell Operating Companies" and "BOCs" mean the corporations listed in Appendix A attached to this Modification of Final Judgment and any entity directly or indirectly owned or controlled by a BOC or affiliated through substantial common ownership.

D. "Carrier" means any person deemed a carrier under the Communications Act of 1934 or amendments thereto, or, with respect to intrastate telecommunications, under the laws of any State.

E. "Customer premises equipment" means equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications, but does not include equipment used to multiplex, maintain, or terminate access lines.

F. "Exchange access" means the provision of exchange services for the purpose of originating or terminating interexchange telecommunications. Exchange access services in-

clude any activity or function performed by a BOC in connection with the origination or termination of interexchange telecommunications, including but not limited to, the provision of network control signalling, answer supervision, automatic calling number identification, carrier access codes, directory services, testing and maintenance of facilities and the provision of information necessary to bill customers. Such services shall be provided by facilities in an exchange area for the transmission, switching, or routing, within the exchange area, of interexchange traffic originating or terminating within the exchange area, and shall include switching traffic within the exchange area above the end office and delivery and receipt of such traffic at a point or points within an exchange area designated by an interexchange carrier for the connection of its facilities with those of the BOC. Such connections, at the option of the interexchange carrier, shall deliver traffic with signal quality and characteristics equal to that provided similar traffic of AT&T, including equal probability of blocking, based on reasonable traffic estimates supplied by each interexchange carrier. Exchange services for exchange access shall not include the performance by any BOC of interexchange traffic routing for any interexchange carrier. In the reorganization specified in section I, trunks used to transmit AT&T's traffic between end offices and class 4 switches shall be exchange access facilities to be owned by the BOCs.

G. "Exchange area," or "exchange" means a geographic area established by a BOC in accordance with the following criteria:

1. any such area shall encompass one or more contiguous local exchange areas serving common social, economic, and other purposes, even where such configuration transcends municipal or other local governmental boundaries;

2. every point served by a BOC within a State shall be included within an exchange area;

3. no such area which includes part or all of one standard metropolitan statistical area (or a consolidated statistical area, in the case of densely populated States) shall include a substantial part of any other standard metropolitan statistical area (or a consolidated statistical area, in the

case of densely populated States), unless the Court shall otherwise allow; and

4. except with approval of the Court, no exchange area located in one State shall include any point located within another State.

H. "Information" means knowledge or intelligence represented by any form of writing, signs, signals, pictures, sounds, or other symbols.

I. "Information access" means the provision of specialized exchange telecommunications services by a BOC in an exchange area in connection with the origination, termination, transmission, switching, forwarding or routing of telecommunications traffic to or from the facilities of a provider of information services. Such specialized exchange telecommunications services include, where necessary, the provision of network control signalling, answer supervision, automatic calling number identification, carrier access codes, testing and maintenance of facilities, and the provision of information necessary to bill customers.

J. "Information service" means the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information which may be conveyed via telecommunications, except that such service does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.

K. "Interexchange telecommunications" means telecommunications between a point or points located in one exchange telecommunications area and a point or points located in one or more other exchange areas or a point outside an exchange area.

L. "Technical information" means intellectual property of all types, including, without limitation, patents, copyrights, and trade secrets, relating to planning documents, designs, specifications, standards, and practices and procedures, including employee training.

N. "Telecommunications equipment" means equipment, other

than customer premises equipment, used by a carrier to provide telecommunications services.

O. "Telecommunications" means the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received, by means of electromagnetic transmission, with or without benefit of any closed transmission medium, including all instrumentalities, facilities, apparatus, and services (including the collection, storage, forwarding, switching, and delivery of such information) essential to such transmission.

P. "Telecommunications service" means the offering for hire of telecommunications facilities, or of telecommunications by means of such facilities.

Q. "Transmission facilities" means equipment (including without limitation wire, cable, microwave, satellite, and fibre-optics) that transmit information by electromagnetic means or which directly support such transmission, but does not include customer premises equipment.

## V

## Compliance Provisions

The defendants, each BOC, and affiliated entities are ordered and directed to advise their officers and other management personnel with significant responsibility for matters addressed in this Modification of Final Judgment of their obligations hereunder. Each BOC shall undertake the following with respect to each such officer or management employee:

1. The distribution to them of a written directive setting forth their employer's policy regardng compliance with the Sherman Act and with this Modification of Final Judgment, with such directive to include:

(a) an admonition that non-compliance with such policy and this Modification of Final Judgment will result in appropriate disciplinary action determined by their employer and which may include dismissal; and

(b) advice that the BOCs' legal advisors are available

at all reasonable times to confer with such persons regarding any compliance questions or problems;

2. The imposition of a requirement that each of them sign and submit to their employer a certificate in substantially the following form:

> The undersigned hereby (1) acknowledges receipt of a copy of the 1982 *United States* v. *Western Electric* Modification of Final Judgment and a written directive setting forth Company policy regarding compliance with the antitrust laws and with such Modification of Final Judgment, (2) represents that the undersigned has read such Modification of Final Judgment and directive and understands those provisions for which the undersigned has responsibility, (3) acknowledges that the undersigned has been advised and understands that non-compliance with such policy and Modification of Final Judgment will result in appropriate disciplinary measures determined by the Company and which may include dismissal, and (4) acknowledges that the undersigned has been advised and understands that non-compliance with the Modification of Final Judgment may also result in conviction for contempt of court and imprisonment and/or fine.

## VI

## Visitorial Provisions

A. For the purpose of determining or securing compliance with this Modification of Final Judgment, and subject to any legally recognized privilege, from time to time:

1. Upon written request of the Attorney General or of the Assistant Attorney General in charge of the Antitrust Division, and on reasonable notice to a defendant or after the reorganization specified in section I, a BOC, made to its principal office, duly authorized representatives of the Department of Justice shall be permitted access during office hours of such defendants or BOCs to depose or interview officers, employees, or agents, and inspect and copy all books, ledgers, accounts, correspondence, memoranda and other records and documents in the possession

or under the control of such defendant, BOC, or subsidiary companies, who may have counsel present, relating to any matters contained in this Modification of Final Judgment; and

2. Upon the written request of the Attorney General or of the Assistant Attorney General in charge of the Antitrust Division made to a defendant's principal office or, after the reorganization specified in section I, a BOC, such defendant, or BOC, shall submit such written reports, under oath if requested, with respect to any of the matters contained in this Modification of Final Judgment as may be requested.

B. No information or documents obtained by the means provided in this section shall be divulged by any representative of the Department of Justice to any person other than a duly authorized representative of the Executive Branch of the United States or the Federal Communications Commission, except in the course of legal proceedings to which the United States is a party, or for the purpose of securing compliance with this Final Judgment, or as otherwise required by law.

C. If at the time information or documents are furnished by a defendant to plaintiff, such defendant or BOC represents and identifies in writing the material in any such information or documents to which a claim of protection may be asserted under Rule 26(c)(7) of the Federal Rules of Civil Procedure, and said defendant or BOC marks each pertinent page of such material, "Subject to claim of protection under Rule 26(c)(7) of the Federal Rules of Civil Procedure," then 10 days' notice shall be given by plaintiff to such defendant or BOC prior to divulging such material in any legal proceeding (other than a grand jury proceeding) to which that defendant or BOC is not a party.

## VII

## Retention of Jurisdiction

Jurisdiction is retained by this Court for the purpose of enabling any of the parties to this Modification of Final Judgment, or, after the reorganization specified in section I,

a BOC to apply to this Court at any time for such further orders or directions as may be necessary or appropriate for the construction or carrying out of this Modification of Final Judgment, for the modification of any of the provisions hereof, for the enforcement of compliance herewith, and for the punishment of any violation hereof.

## VIII

### MODIFICATIONS

A. Notwithstanding the provisions of section II(D)(2), the separated BOCs shall be permitted to provide, but not manufacture, customer premises equipment.

B. Notwithstanding the provisions of section II(D)(3), the separated BOCs shall be permitted to produce, publish, and distribute printed directories which contain advertisements and which list general product and business categories, the service or product providers under these categories, and their names, telephone numbers, and addresses.

Notwithstanding the provisions of sections I(A)(1), I(A)(2), I(A)(4), all facilities, personnel, systems, and rights to technical information owned by AT&T, its affiliates, or the BOCs which are necessary for the production, publication, and distribution of printed advertising directories shall be transferred to the separated BOCs.

C. The restrictions imposed upon the separated BOCs by virtue of section II(D) shall be removed upon a showing by the petitioning BOC that there is no substantial possibility that it could use its monopoly power to impede competition in the market it seeks to enter.

D. AT&T shall not engage in electronic publishing over its own transmission facilities. "Electronic publishing" means the provision of any information which AT&T or its affiliates has, or has caused to be, originated, authored, compiled, collected, or edited, or in which it has a direct or indirect financial or proprietary interest, and which is disseminated to an unaffiliated person through some electronic means.

Nothing in this provision precludes AT&T from offering

electronic directory services that list general product and business categories, the service or product providers under these categories, and their names, telephone numbers, and addresses; or from providing the time, weather, and such other audio services as are being offered as of the date of the entry of the decree to the geographic areas of the country receiving those services as of that date.

Upon application of AT&T, this restriction shall be removed after seven years from the date of entry of the decree, unless the Court finds that competitive conditions clearly require its extension.

E. If a separated BOC provides billing services to AT&T pursuant to Appendix B(C)(2), it shall include upon the portion of the bill devoted to interexchange services the following legend:

> This portion of your bill is provided as a service to AT&T. There is no connection between this company and AT&T. You may choose another company for your long distance telephone calls while still receiving your local telephone service from this company.

F. Notwithstanding the provisions of Appendix B(C)(3), whenever, as permitted by the decree, a separated BOC fails to offer exchange access to an interexchange carrier that is equal in type and quality to that provided for the interexchange traffic of AT&T, the tariffs filed for such less-than-equal access shall reflect the lesser cost, if any, of such access as compared to the exchange access provided AT&T.

G. Facilities and other assets which serve both AT&T and one or more BOCs shall be transferred to the separated BOCs if the use made by such BOC or BOCs predominates over that of AT&T. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

H. At the time of the transfer of ownership provided for in section I(A)(4), the separated BOCs shall have debt ratios of approximately forty-five percent (except for Pacific Telephone and Telegraph Company which shall have a debt ratio of approximately fifty percent), and the quality of the debt

shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

I. The Court may act *sua sponte* to issue orders or directions for the construction or carrying out of this decree, for the enforcement of compliance therewith, and for the punishment of any violation thereof.

J. Notwithstanding the provisions of section I(A), the plan of reorganization shall not be implemented until approved by the Court as being consistent with the provisions and principles of the decree.

Entered this _____ day of _____, 1982.

United States District Judge

S/_____
Harold H. Greene
United States District Judge

## APPENDIX A

Bell Telephone Company of Nevada

Illinois Bell Telephone Company

Indiana Bell Telephone Company, Incorporated

Michigan Bell Telephone Company

New England Telephone and Telegraph Company

New Jersey Bell Telephone Company

New York Telephone Company

Northwestern Bell Telephone Company

Pacific Northwest Bell Telephone Company

South Central Bell Telephone Company

Southern Bell Telephone and Telegraph Company

Southwestern Bell Telephone Company

The Bell Telephone Company of Pennsylvania

The Chesapeake and Potomac Telephone Company

The Chesapeake and Potomac Telephone Company of Maryland

The Chesapeake and Potomac Telephone Company of Virginia

The Chesapeake and Potomac Telephone Company of West Virginia

The Diamond State Telephone Company

The Mountain States Telephone and Telegraph Company

The Ohio Bell Telephone Company

The Pacific Telephone and Telegraph Company

Wisconsin Telephone Company

## APPENDIX B

### PHASED-IN BOC PROVISION OF EQUAL EXCHANGE ACCESS

A. 1. As part of its obligation to provide non-discriminatory access to interexchange carriers, no later than September 1, 1984, each BOC shall begin to offer to all interexchange carriers exchange access on an unbundled, tariffed basis, that is equal in type and quality to that provided for the interexchange telecommunications services of AT&T and its affiliates. No later than September 1, 1985, such equal access shall be offered through end offices of each BOC serving at least one-third of that BOC's exchange access lines and, upon bona fide request, every end office shall offer such access by September 1, 1986. Nothing in this Modification of Final Judgment shall be construed to permit a BOC to refuse to provide to any interexchange carrier or information service provider, upon bona fide request, exchange or information access superior or inferior in type or quality to that provided for AT&T's interexchange services or information services at charges reflecting the reduced or increased cost of such access.

2. (i) Notwithstanding paragraph (1), in those instances in which a BOC is providing exchange access for Message Telecommunications Service on the effective date of this Modification of Final Judgment through access codes that do not permit the designation of more than one interexchange carrier, then, in accordance with the schedule set out in paragraph (1), exchange access for additional carriers shall be provided through access codes containing the minimum number of digits necessary at the time access is sought to permit nationwide, multiple carrier designation for the number of interexchange carriers reasonably expected to require such designation in the immediate future.

(ii) Each BOC shall, in accordance with the schedules set out in paragraph (1), offer as a tariffed service exchange access that permits each subscriber automatically to route, with the use of access codes, all the subscriber's interexchange communications to the interexchange carrier of the customer's designation.

(iii) At such time as the national numbering area (area code) plan is revised to require the use of additional digits, each BOC shall provide exchange access to every interexchange carrier, including AT&T, through a uniform number of digits.

3. Notwithstanding paragraphs (1) and (2), with respect to access provided through an end office employing switches technologically antecedent to electronic, stored program control switches or those offices served by switches that characteristically serve fewer than 10,000 access lines, a BOC may not be required to provide equal access through a switch if, upon complaint being made to the Court, the BOC carries the burden of showing that for particular categories of services such access is not physically feasible except at costs that clearly outweigh potential benefits to users of telecommunications services. Any such denial of access under the preceding sentence shall be for the minimum divergence in access necessary, and for the minimum time necessary, to achieve such feasibility.

B. 1. The BOCs are ordered and directed to file, to become effective on the effective date of the reorganization described in paragraph I(A)(4), tariffs for the provision of exchange access including the provision by each BOC of exchange access for AT&T's interexchange telecommunications. Such tariffs shall provide unbundled schedules of charges for exchange access and shall not discriminate against any carrier or other customer. Such tariffs shall replace the division of revenues process used to allocate revenues to a BOC for exchange access provided for the interexchange telecommunications of BOCs or AT&T.

2. Each tariff for exchange access shall be filed on an unbundled basis specifying each type of service, element by element, and no tariff shall require an interexchange carrier to pay for types of exchange access that it does not utilize. The charges for each type of exchange access shall be cost justified and any differences in charges to carriers shall be cost justified on the basis of differences in services provided.

3. Notwithstanding the requirements of paragraph (2), from the date of reorganization specified in section I until

September 1, 1991, the charges for delivery or receipt of traffic of the same type between end offices and facilities of interexchange carriers within an exchange area, or within reasonable subzones of an exchange area, shall be equal, per unit of traffic delivered or received, for all interexchange carriers; provided, that the facilities of any interexchange carrier within five miles of an AT&T class 4 switch shall, with respect to end offices served by such class 4 switch, be considered to be in the same subzone as such class 4 switch.

4. Each BOC offering exchange access as part of a joint or through service shall offer to make exchange access available to all interexchange carriers on the same terms and conditions, and at the same charges, as are provided as part of a joint or through service, and no payment or consideration of any kind shall be retained by the BOC for the provision of exchange access under such joint or through service other than through tariffs filed pursuant to this paragraph.

C. 1. Nothing in this Modification of Final Judgment shall be construed to require a BOC to allow joint ownership or use of its switches, or to require a BOC to allow co-location in its building of the equipment of other carriers. When a BOC uses facilities that (i) are employed to provide exchange telecommunications or exchange access or both, and (ii) are also used for the transmission or switching of interexchange telecommunications, then the costs of such latter use shall be allocated to the interexchange use and shall be excluded from the costs underlying the determination of charges for either of the former uses.

2. Nothing in this Modification of Final Judgment shall either require a BOC to bill customers for the interexchange services of any interexchange carrier or preclude a BOC from billing its customers for the interexchange services of any interexchange carrier it designates, provided that when a BOC does provide billing services to an interexchange carrier, the BOC may not discontinue local exchange service to any customer because of nonpayment of interexchange charges unless it offers to provide billing services to all interexchange carriers, and provided further that the BOC's cost of any

such billing shall be included in its tariffed access charges to that interexchange carrier.

3. Whenever, as permitted by this Modification of Final Judgment, a BOC fails to offer exchange access to an interexchange carrier that is equal in type and quality to that provided for the interexchange traffic of AT&T, nothing in this Modification of Final Judgment shall prohbibit the BOC from collecting reduced charges for such less-than-equal exchange access to reflect the lesser value of such exchange access to the interexchange carrier and its customers compared to the exchange access provided AT&T.

ORDER ADMITTING INTERVENORS

(Entered: August 26, 1982)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

| | |
|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

ORDER

Upon consideration of the motions to intervene, the memoranda submitted in support thereof, and the entire record herein, and for the reasons stated in this Court's opinion of August 11, 1982, it is this 26th day of August, 1982,

ORDERED

1. The motions to intervene be and they are hereby granted, and the following persons and organizations are hereby permitted to intervene:

Ad Hoc Telecommunications Users Committee; American Newspaper Publishers Association; American Petroleum Institute; American Satellite Company; Associated Telephone Answering Exchanges, Inc.; Association of American Railroads; Association of Data Communications Users; Association of Data Processing Service Organizations; Audichron Company; Black Citizens for a Fair Media; California Hispanics; Citizens Utilities Company; Communication Commission of the National Council of the Churches of Christ in the USA; Communications Workers of America; Compuserve, Inc.; Computer and Business Equipment Manufacturers Association; Computer and Communications Industry Association; Compuserve, Inc.; Congress Watch; Continental Telecom, Inc.; D/FW Signal, Inc.; Education and Cultivation Division of the General Board of Global Ministries of the United Methodist Church; Federal Communications Commission; General Dynamics Communications Co.; General Telephone & Electronics Corp.; Independent Data Communications Manufacturers Association; Independent Telecommunications Suppliers' Council; International Telephone and Telegraph Corp.; Jack Faucett Associates, Inc., et al.; Leghorn Telepublishing Co.; MCI Communications Corp.; Mobile Marine Radio, Inc.; National Association for the Advancement of Colored People; National Association for Better Broadcasting; National Association of Broadcasters; National Association of Regulatory Utility Commissioners; National Association of State Utility Consumer Advocates; Na-

tional Cable Television Association; National Catholic Broadcasters Association; National Citizens Committee for Broadcasting; National Latino Media Coalition; National Newspaper Association; North American Telephone Association; Northeastern Telephone Co.; Office of Communication of the United Church of Christ; Reformed Church in America; Rogers Radio Communication Services, Inc.; Rural Telephone Coalition; San/Bar Corp.; Satellite Business Systems; Sonitrol Distributers Council, Inc.; Southern Pacific Communications Co.; Sperry Corporation; Stromberg-Carlson Corp.; Tandy Corporation; Telocator Network of America; U.S. Telephone Communications, Inc.; United States Independent Telephone Association; United States Telecommunications Suppliers Association; United Telecommunications, Inc.; Utilities Telecommunications Council; Warner Amex Cable Communications, Inc.; Western Union Telegraph Co.; Westinghouse Broadcasting and Cable, Inc.; States of Arizona, California, Colorado, Delaware, Illinois, Maine, Maryland, Michigan, Missouri, New Mexico, New Hampshire, New York, North Carolina, Oregon, Pennsylvania, Tennessee, Virginia, Wisconsin; Public Service Commissions of Arkansas, California, District of Columbia, Florida, Idaho, Kentucky, Michigan, Missouri, Montana, Nebraska, Nevada, New York, South Dakota, Utah, West Virginia, Wisconsin, Wyoming; Iowa Commerce Commission; Kansas Corporation Commission; New Mexico Corporation Commission; Office of the Consumers' Counsel, State of Ohio; Oklahoma Corporation Commission; Virginia State Corporation Commission; Washington Utilities and Transportation Commission; City of Cincinnati; City of New York.

2. The intervenors shall have the following rights:

a. the right to appeal this Court's decision to enter the consent decree in Civil Action No. 82-0192 and to dismiss Civil Action No. 74-1698; and, if an appeal is taken by another intervenor, the right, to the extent permitted by the reviewing courts, to support this Court's decisions on appeal;

b. the right to participate fully in proceedings to be established by this Court to determine whether the plan of reorganization filed pursuant to the consent decree should be approved; and

c. the right to appeal this Court's decision concerning such plan of reorganization; and, if an appeal is taken, the right, to the extent permitted by the reviewing courts, to support this Court's decision on appeal.

3. Intervenor status shall terminate in this Court with the entry of this Court's decision concerning the plan of reorganization, and, more generally, following appellate review of the Court's decision concerning such plan.

S/_____
Harold H. Greene
United States District Judge

OPINION

(Filed: July 8, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

| | |
|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

## OPINION

Section I(A) of the decree entered on August 24, 1982, provides that "[n]ot later than six months after the effective date of [the decree], defendant AT&T shall submit to the Department of Justice for its approval, and thereafter implement, a plan of reorganization," and section VIII(J) specifies that the plan of reorganization "shall not be implemented until approved by the Court as being consistent with the provisions and principles of the decree." In accordance with these provisions, AT&T has submitted its plan to the Court following approval

by the Department of Justice.[1] The intervenors were thereafter given the opportunity to raise objections; a considerable number of such objections were, in fact, filed with the Court; and AT&T and the Department of Justice, in turn, filed their own responses.

Following receipt of these papers, the Court designated certain issues for more intensive briefing and for oral argument.[2] Voluminous briefs were received on these issues, and argument was had thereon on June 2, 1983.[3] At that hearing, the Court also heard testimony from three of the designated chief executives[4] of the seven newly-established Regional Companies.[5] Additional documents were submitted after the hearing, including one—a letter with attachments from AT&T (see p. 208 *infra*)—as late as June 29, 1983.

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[1] The Department required certain modifications which AT&T accepted.

[2] The Court, of course, considered all the provisions of the plan, including those which were not set down for hearing.

[3] The four issues addressed by counsel were the allocation of the costs of equal access, the distribution of contingent liabilities arising from antitrust suits against AT&T, assignment of the Bell name and logo, and assignment of patents. Three opponents of the plan of reorganization focused on the first two issues: MCI Communications Corp., the Church of Christ *et al.*, and the National Association of Regulatory and Utility Commissioners (NARUC); three opponents focused on the last two issues: Tandy Corp., Black Citizens for a Fair Media *et al.*, and NARUC. AT&T and the Department of Justice argued in favor of the plan of reorganization on all four issues.

[4] Zane Barnes, chief executive-designate of the Southwestern Region, testified about the costs of equal access and the assignment of switching systems. William Weiss, chief executive-designate of the Midwest Region, testified about the apportionment of contingent liabilities and the proposed Central Staff Organization. Thomas Bolger, chief executive-designate of the Mid-Atlantic Region, testified about assignment of the Bell name and logo, and assignment of patents.

[5] The seven Regional Companies will be holding companies for the twenty-two Bell Operating Companies. The Northeast Region will include New England Telephone Co. and New York Telephone Co. The Mid-Atlantic Region will include New Jersey Bell Telephone Co., the

The Court has considered all issues raised with respect to the plan of reorganization on the basis of the written materials, the oral hearing, the testimony, and the entire record herein, and it has concluded that the plan of reorganization will be approved[6] provided that certain inconsistencies with the provisions and principles of the decree are corrected.[7]

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Bell Telephone Company of Pennsylvania, the Diamond State Telephone Company, and the Chesapeake and Potomac Telephone Companies of Washington, D. C., Virginia, Maryland, and West Virginia. The Southern Region will include Southern Bell Telephone and Telegraph Co. and South Central Bell Telephone Company. The Midwest Region will include the Ohio Bell Telephone Co., Michigan Bell Telephone Co., Indiana Bell Telephone Co., Illinois Bell Telephone Co., and Wisconsin Telephone Co. The Mountain-Northwest Region will include Northwestern Bell Telephone Co., the Mountain States Telephone and Telegraph Co., and Pacific Northwest Bell Telephone Co. The Far West Region will include the Pacific Telephone and Telegraph Co. and Bell Telephone Company of Nevada. The Southwest Regio will include Southwestern Bell Telephone Co. Although the Regional Companies have been identified by geographic designations throughout these proceedings, they will subsequently be adopting formal corporate names. For instance, the Northeast Region has announced that it will call itself NYNEX, while the Mountain-Northwest Region has chosen U.S. West. Except where the distinction appears to be significant, the Regional Companies and the Operating Companies will be referred to herein as the Operating Companies.

[6] On April 20, 1983, the Court tentatively approved the Local Access and Transport Areas (LATAs) within which the Operating Companies' telecommunications services will be confined. See *United States* v. *Western Electric Co. and American Telephone & Telegraph Co.*, 1983-1 Trade Cas. ¶65,333 (D.D.C. April 20, 1983). The LATA applications were technically the first phase of the plan of reorganization. The parties proposed, and the Court accepted, that review of the plan of reorganization be undertaken in two stages for the sake of speed and convenience and because the drawing of geographic boundaries naturally preceded any division of assets between AT&T and the Operating Companies. Remaining issues with respect to the LATAs are considered in Part VII *infra*.

[7] Both AT&T and the Department have filed motions for approval of the plan of reorganization. Those motions will be acted upon after the required modifications are submitted to the Court.

## I

### EQUAL ACCESS

The decree requires the Operating Companies to "provide to all interexchange carriers and information service providers exchange access, information access, and exchange services for such access . . . that is equal in type, quality, and price to that provided to AT&T and its affiliates." Section II(A).[8] As the stepping stone to increased competition in the field of intercity telecommunications, the decree's equal access requirements and the implementing provisions of the plan of reorganization have generated substantial controversy. Comments filed by Operating Company executives, interexchange carriers, regulatory commissions, consumer groups, and telecommunications associations indicate that at this stage of the proceedings[9] there is a need to resolve three primary questions relating to equal access:[10] what is it, how is it to be achieved, and who will pay for it?

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[8] The equal access obligation takes effect on September 1, 1984, and it will be phased in over a two-year period. By September 1, 1985, the Operating Companies must provide equal access to one-third of their respective access lines, and by September 1, 1986, to the remaining access lines. See Appendix B to the decree.

[9] Under Section II(C) of the decree, the Operating Companies are not required to file their precise plans for providing equal access until six months after divestiture. That date may be unrealistically late because much of the preparation that must be completed by September 1984 cannot be undertaken by the Operating Companies until they are told whether their initial plans are acceptable. See Response of the United States to Public Comments and Action on AT&T's Proposed Plan of Reorganization, filed March 24, 1983 (hereinafter Department of Justice Response to Comments) at 187-88.

[10] These issues bear, *inter alia*, on the assignment of assets and liabilities between AT&T and the Operating Companies, and they are therefore properly considered as part of the plan of reorganization.

A. What Does "Equal" Mean?

A number of the Operating Companies propose to connect AT&T's interexchange competitors to the homes or businesses of local telephone subscribers by using facilities built or upgraded specifically for that purpose; AT&T, on the other hand, will in numerous LATAs gain access to subscriber lines through different facilities, many of which are already extant.[11] For that reason, the access provided AT&T's competitors will not be identical to that given AT&T in all places; rather, it will be technically different in certain areas and at certain times.

The Operating Companies assert that any such technical deviations will be so slight as to be imperceptible to all customers, whether of voice or of data.[12] Accordingly, they urge the Court to accept a definition of "equal access" as access whose "overall quality in a particular area is equal within a reasonable range which is applicable to all carriers,"[13] and to reject a more stringent definition which would demand access that yields identical technical quality (*i.e.*, identical values for loss, noise, and echo, and identical possibility of blocking).[14]

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[11] In only one of the seven telephone regions will this not occur. In the Northeast Region, which encompasses New York and New England, AT&T and its competitors will be served from the same switches in the same LATAs. Response of the Northeast Region to the Court's May 17, 1983 Memorandum at 2 n.**.

[12] It is asserted that even the interexchange carriers will not be able to detect any qualitative difference.

[13] Statement of the Operating Companies Supplementing their Responses to the Court's Memorandum of May 17, 1983 Regarding the No. 4ESS Switching Systems (hereinafter Operating Company Supplement) at 2.

[14] The Operating Companies state that identical per call access would be impossible, even if a uniform access configuration were imposed in each LATA, because of "normal variations of electrical characteristics of facility components and installation line-up variations. . . ." Operating Company Supplement at 3.

The Court accepts the Operating Companies' definition and will not insist on absolute technical equality. To do otherwise would necessitate substantial dismantling and reconstruction of local telephone networks without any real benefits either to the consuming public or to AT&T's intercity competitors. This ruling, however, is based squarely upon the Operating Companies' representations that both voice and data customers will perceive no qualitative differences between AT&T transmissions and those of its competitors—at least with respect to those portions of the transmissions carried by an Operating Company.[15] The Operating Companies are well aware, however, that the Department of Justice will be monitoring the quality of the access they will provide and that the price of falling short of their assurance of equal quality will be enforcement proceedings brought by the Department.[16]

The interexchange competitors, as noted, would not be disadvantaged if the Operating Companies meet the standard they have proposed. Their real complaint is that the Operating Companies will be unable to meet that standard in many of the LATAs by the means they propose[17]—a subject to which the Court now turns.

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[15] The Operating Companies are not responsible, of course, for correcting any quality deficiencies that may result from an interexchange carrier's own facilities.

[16] See Department of Justice Response to Comments at 187.

[17] The skepticism of the interexchange competitors relates largely to the kinds of switches the Operating Companies will employ to connect the competing interexchange networks with the local Operating Company networks. See 1983-1 Trade Cas. ¶65,333.

B. Which Switches Should Be Used for Access Arrangements?

First. Since the initial comments were filed regarding the first, or LATA, phase of the plan of reorganization, a number of intervenors have expressed concern over the kinds of switches the Operating Companies will use to route traffic from an interexchange carrier's point of presence in a LATA to a local Class 5 end office.[18]

The Court initially shared this concern, primarily because so little information about equal access planning for individual LATAs had been made available. In May of 1983, it therefore requested the Regional Companies to report in detail regarding their plans for equal access and their need in this respect for the efficient, state-of-the-art No. 4ESS switches.[19] The Court asked to be ap-

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[18] An end office is the plant into which individual subscribers' telephone access lines feed. It is typically the point of concentration of telecommunications traffic closest to the subscriber—*i.e.*, the point of origination or termination—and it is decidedly local in character and function. In the Bell System hierarchy of functions, this is the facility which performs the Class 5 function, meaning that from the Class 5 end office a call is either routed directly to another end office through a Class 5 trunk (a "local" call) or it is routed to a Class 4 facility for interconnection with the "toll" network. In a number of sites, the Class 4 and Class 5 functions are located in the same facility. Under the plan of reorganization, all such facilities will be owned by the Operating Companies because of the local nature of the Class 5 function. Plan of reorganization at 16-17.

[19] There are 91 such switches in the Bell System. They were first introduced in 1976 and are large, four-wire digital switches with the capacity to handle almost 700,000 call attempts per hour. Memorandum of the Midwest Regional Holding Company, May 31, 1983, at 3. The DMS-200, DMS-100/200, and the No. 5ESS switches are smaller than the No. 4ESS, but they "provide equivalent transmission and switching characteristics as the No. 4ESS." Response of Donald E. Guinn to the Court's Memorandum of May 17, 1983, at 3 n.*. These four switches are the most advanced of all switches in use today.

prised of any instances where an Operating Company believed that a particular switch should be assigned to it for equal access purposes even though that switch would belong to AT&T under the predominant use test.[20] The responses were extremely helpful. Their detail and the varied recommendations made with respect to each region revealed that, contrary to some speculation, the Operating Companies had carefully studied the alternatives for the provision of access within their respective territories, and that they had concluded, independent of pressure from AT&T, which arrangements would be most economical and efficient for them.

Most of the LATAs will be served by four-wire digital tandems,[21] if not in 1984, then within two years.[22] The Operating Companies are not planning to make as much use of the existing No. 4ESS switches, however, as might have been anticipated. The basis of that choice appears reasonable.

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[20] Bell System assets will be distributed according to the function they perform. 552 F. Supp. at 206. Those assets performing exchange and exchange access functions will be owned by the Operating Companies; those performing interexchange functions by AT&T and its affiliates. Section I(A)(1). About eighty percent of the Bell System's assets perform one function or the other and hence are classifiable with relative ease. The remaining 20 percent are multifunction assets, providing both exchange and interexchange services. The government proposed, and the Court accepted, that the predominant use test be applied to these assets, that is, the asset will be assigned to the entity whose use predominates. 552 F. Supp. at 207. The Court noted, however, that in certain cases the test would be inappropriate (552 F. Supp. at 207 n.317) as where a facility primarily used in connection with interexchange services was necessary for the provision of equal access by an Operating Company. See 552 F. Supp. at 200-01; section VIII(G) of the decree.

[21] These are the advanced switches of the type described in note 19 *supra* and are the switches most readily connected to the four-wire trunks which the interexchange carriers primarily use in their own networks. Pacific and Nevada Bell will use "state of the art digital, four-wire tandems for more than 99 percent of [their] requirements." Response of Donald E. Guinn at 8 n.*. This appears to be true for

Because of the large capacity of the No. 4ESS switch, the cost to an Operating Company of leasing part of it would be, in most cases, greater than would be that of constructing a smaller-scale switch directly for that company. The other alternative—vesting ownership of the No. 4ESS switch in the Operating Company, in the expectation that it will be able to lease substantial capacity to AT&T—is problematic in many cases because AT&T may choose instead to build a new switch (and even if it did not, it would be required in any event under the plan to terminate the lease after eight years). In either event, the Operating Company would thus be left with the expense of stranded capacity.

For these reasons, the Operating Companies will instead engage in a substantial amount of new construction, and they have persuaded the Court that this is an appropriate decision. In some instances they will thereby be merely accelerating construction which would have occurred in any event, and new construction, as opposed to leasing, will have the advantage of facilitating network separation between AT&T and the Operating Companies.

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New York and New England as well. In the remaining five regions, it appears that all switches to be constructed will be four-wire digital tandems. Only in a relatively small number of LATAs do the companies propose to provide access via two-wire switches. This, and the fact that the Department of Justice will continue to study whether two-wire switches can provide suitable access, largely moots the concerns of Satellite Business Systems, Southern Pacific Communications Corp., and MCI Communications Corp. that the Operating Companies would make larger scale use of two-wire switches, necessitating the use of adapters to connect them to the four-wire trunks of the interexchange competitors.

[22] AT&T has consistently maintained that requiring interexchange competitors to hook into two-wire switches via adaptors would not impair the quality of the transmissions, a point which AT&T's competitors have just as consistently challenged. Since the Operating Companies have decided to offer mainly four-wire connections, this dispute is largely moot. See note 21 *supra*.

Given the care which went into the Operating Companies' studies, the Court will not second-guess them by imposing upon them an assignment of switches which they do not endorse. The Court therefore rejects the position of some[23] that all No. 4ESS switches should be divested from AT&T and assigned instead to the Operating Companies.

Second. The New England Telephone Co. (NET) has suggested that it could provide access more economically if the Court were to override the predominant use test in its territory with respect to three advanced switching systems. NET wishes to make extensive use of No. 4ESS switches—which apparently would be more appropriate in its region than elsewhere because of existing population densities—and it states that it could benefit from the allocation of three existing No. 4ESS switches (in Manchester, New Hampshire; Springfield, Massachusetts; and Cambridge, Massachusetts).[24] NET has further informed the Court that if it were to receive the existing switches in these locations, the net present value advantage to it would range from $20 to $25 million with respect to the Cambridge switch and from zero to $8 million per switch with respect to the Manchester and Springfield facilities.[25]

Although it accepted the predominant use test, the Court has stated that this test would be waived where particular equipment was needed by an Operating Company for the provision of equal access. See note 20

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[23] *E.g.*, Black Citizens for a Fair Media, *et al.*

[24] NET states that owning the switches, and presumably leasing space to AT&T, would in these instances be the cheapest alternative. The next best option would be for NET to build its own 4ESS switches, with the most costly alternative being to lease space from AT&T. Response of the Northeast Region, May 31, 1983, at 5-6.

[25] Different values are achieved depending upon the assumptions used.

*supra*. Clearly that need is present with respect to the Cambridge switch,[26] and the Court will therefore require that AT&T assign that switch to NET. The matter is not as clear with regard to the Manchester and Springfield switches. If NET wishes to make a formal proposal for the transfer of these switches, it should submit a motion explaining under what circumstances the savings would amount to zero and under what circumstances they would amount to $8 million,[27] and AT&T and the Department of Justice may respond to the motion. The Court will order no other changes in the assignment of switches.[28]

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[26] The expenditure of $20 to $25 million required for the construction of a new switch is not an acceptable alternative.

[27] NET should also indicate whether assignment to it of the Cambridge switch would alter its analysis of the impact of a separate Worcester LATA. Specifically, if NET owns the Cambridge switch would it also want to build a Framingham No. 4ESS switch?

[28] The Court notes that Bell of Pennsylvania has supplanted its proposal to use a 1AESS switch to offer access in Harrisburg (the "Capital" LATA) with a plan to build a DMS-200, 4ESS or comparable four-wire switch by September 1985. Response of the Mid-Atlantic Bell Telephone Companies, May 31, 1983, at 6 n.6. Bell of Pennsylvania also intends to offer access to the Philadelphia LATA through the existing 4ESS until its own digital switch is in place, assuming that "billing software develops satisfactorily." *Id.* These plans are hereby approved. The Court accepts Pacific Northwest Bell's proposal to build its own digital switch in Seattle and use direct trunking to provide access pending completion of the switch. See Appendix A to Response of Operating Companies in Mountain-Northwest Region to Court's Memorandum of May 17, 1983.

The suggestion of the Department of Justice that the date for the Operating Companies' formal equal access filings be advanced is a sound one. The Department should consult with the Operating Companies with regard to the timing of an accelerated schedule.

C. How Should the Operating Companies Recover the Costs of Becoming Equal Access Providers and of Reconfiguring Local Networks to Conform to LATA Boundaries?

AT&T estimates that it will cost the Operating Companies $73 million to reconfigure their networks[29] and $2.47 billion to provide equal access.[30] The plan of reorganization does not directly address the issue of who should pay these costs but seems to proceed on the premise that equal access is exclusively an Operating Company responsibility with which the plan, and AT&T, need not be concerned. That approach is improperly simplistic.

Section I(A)(1) of the decree states that AT&T shall

> transfer from AT&T and its affiliates to the BOCs . . . sufficient facilities [and] systems . . . to permit the BOCs to perform, independently of AT&T, exchange telecommunications and exchange access functions . . . and [which are] *sufficient to enable the BOCs to meet the equal exchange access requirements* of Appendix B (emphasis added).

There can be no doubt, then, that AT&T has a significant responsibility[31] to see to it that the Operating

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[29] It is obvious that this figure is somewhat low, as is indicated, for example, by the claim of the Mid-Atlantic Region that the estimate of $73 million does not include any of the $30 million it expects to spend on network reconfiguration. Response of the Mid-Atlantic Bell Telephone Companies, May 31, 1983, at 9 n.10.

[30] AT&T Memorandum, May 23, 1983, at 4 n.**, 5 n.*. This includes putting in place access tandems for interconnection between interexchange carriers' points of presence and the local loops, plus any direct trunks from points of presence to end offices where this is considered more efficient than using access tandems. The exact amount will depend on many factors, including any waivers of the equal access requirements pursuant to Appendix B of the decree.

[31] The primary responsibility lies with the Operating Companies since as part of the divestiture process they will receive the Bell System's local exchange facilities by which equal access will be provided.

Companies are left in a position, as of divestiture, that will enable them to offer equal access to AT&T's competitors.[32] The only question is what obligations attach to this responsibility.

The intervenors have proposed various ways to assign the costs of network configuration and equal access directly to AT&T, from requiring AT&T to give the Operating Companies more switches to requiring it to finance all equal access projects. The former has the disadvantage of imposing switch assignments on the Operating Companies which they do not want; the latter is problematic in that it will perpetuate a liaison between AT&T and the Operating Companies where none should exist. AT&T, for its part, while it rejects any suggestion that it should have to pay these costs, in effect concedes that it bears some share of the responsibility since it asserts that the access charges paid by interexchange carriers will reimburse the Operating Companies, and that it, as the dominant interexchange carrier, will pay the lion's share of such charges.

All the parties have agreed that these costs are properly to be recovered from the interexchange carriers, rather than through access charges levied on local ratepayers, because the expenditures represent improvements to the long distance network. AT&T's assurances to the contrary notwithstanding, it is unsettled at present by what methodology the interexchange carriers could be made to bear the costs of equal access and network reconfiguration through interstate access charges. Under existing procedures for allocating property costs, revenues, ex-

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[32] It has been clear at least since the decision of the Court of Appeals in *MCI Telecommunications Corp.* v. *FCC*, 580 F.2d 590 (D.C. Cir. 1978) (Execunet II) that AT&T was under an obligation to furnish equal or substantially equal access to its intercity competitors. See also, *United States* v. *Am. Tel. & Tel. Co.*, 524 F. Supp. 1336, 1356, 1360 (D.D.C. 1981).

penses, and reserves between intrastate and interstate jurisdictions for rate making purposes (see 47 C.F.R. §67.1), a disproportionately small amount of equal access and network reconfiguration costs would be designated for recoupment through interstate tariffs; most of these costs would be designated for recovery through intrastate tariffs even though, at least initially, most of the benefits of equal access connections will flow to users of interstate, not intrastate, telecommunications services. See Correspondence between Howard J. Trienens and A. Gary Collins, filed June 29, 1983; Response of Mid-Atlantic Bell Telephone Companies, May 31, 1983, at 8-10.[33] In fact, only after it was pointed out by others did AT&T acknowledge that all equal access and network

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[33] Indeed, the Mid-Atlantic Region expects to spend $200 million for equal access through 1986, but anticipates that, under the existing separations procedures, about 60 percent of these costs would be allocated to intrastate, not interstate, rate-making. As the Mid-Atlantic region states:

> It may be possible, if regulators agree, to apportion these costs more equitably between the interstate and intrastate jurisdictions. If this does not occur, there is no assurance that state regulators will be able to fix intrastate access rates high enough to recover these costs. If rates are fixed at such level, [interexchange carriers] will have a strong incentive to 'forum shop' between interstate and intrastate tariffs and to by-pass the BOCs for intrastate access. Even if the bulk of the costs become properly assigned as between interstate and intrastate access, the possibility of by-pass becomes more threatening with each increase in access costs.

Response of the Mid-Atlantic Bell Telephone Companies, May 31, 1983, at 9-10.

AT&T and the Operating Company personnel apparently are working on a proposal to treat equal access and reconfiguration costs as if they were costs of "Special Services Switching Equipment" which, it is asserted, "will avoid the misallocation of costs to the intrastate jurisdiction" and will allocate investment and related expenses on the basis of relative toll minutes, *i.e.*, on the basis of carriers actually using access services. Letter from A. Gray Collins to Howard J. Trienens, filed June 29, 1983, at 2. The FCC would have to approve any such proposal.

configuration costs would not be recovered through interexchange carrier charges under the current jurisdictional separations procedures.

Another, equally serious problem is created by the ability of AT&T to make use of the so-called bypass technology (552 F. Supp. at 175-76) which would allow that company, at its choice, and given the availability of the necessary technology, to bypass the Operating Company circuits altogether and to reach ultimate telephone subscribers directly. To the extent that bypass is a serious threat to the Operating Companies,[34] AT&T, because of its size and its well-developed telecommunications technology, is by far the most likely origin of that threat. Use of that bypass technology by AT&T would, of course, permit it to escape the payment of access charges to the Operating Companies, and this, in turn, would jeopardize the recovery of the funds which will be expended by the Operating Companies for the equal access and reconfiguration construction program.

It is thus not certain that the Operating Companies will be fully reimbursed through carrier access charges for their equal access and network reconfiguration expenditures. Yet because the decree anticipated that AT&T would transfer sufficient facilities to the Operating Companies to ensure equal access; because it now appears that the Operating Companies will instead have to undertake substantial new construction of their own; and because AT&T has throughout this proceeding assured the Court that access charges paid by interexchange carriers would be the instrument which would prevent divestiture from causing increases in local rates, it is appropriate that AT&T should bear the ultimate risk if it

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[34] The Court, unlike the Federal Communications Commission, does not consider bypass to be an immediate large-scale problem. See transcript June 2, 1983 hearing at 25466.

turns out that its assurances are overly optimistic.[35] That risk will accordingly be assigned to AT&T in the following manner.

According to the plan of reorganization, the equal access construction program will be completed in five years. Within five years thereafter, that is by January 1, 1994, if the Operating Companies have not recovered the costs of equal access and network reconfiguration, inclusive of financing costs, through their collection of access charges from the interexchange carriers,[36] AT&T will be responsible for reimbursing the Operating Companies in the amount of any remaining deficit.[37] A preliminary accounting will take place at the close of the construction program on or by January 1, 1989, whichever is earlier.

If the Operating Companies and AT&T are able to report to the Court on or before January 1, 1994, of their agreement that all costs have been recovered, AT&T will be discharged from any further obligation with respect to the cost of equal access and network reconfiguration. If there is a dispute, the Court will decide, if necessary with

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[35] However, for the reasons stated in note 31 *supra*, there is no basis for requiring AT&T to pay all of these costs, in addition to the contribution it will make by way of the access charges and the costs of the risks assigned to it herein.

[36] AT&T is entitled, in equity, to count toward reimbursement of these costs all carrier access charges, not only the charges collected from it. If only AT&T's contributions were counted, the Operating Companies, AT&T's interexchange competitors, or both, would reap a windfall.

[37] The Operating Companies shall keep records to isolate those expenses incurred solely for equal access and network reconfiguration as mandated by the decree from expenses they would have incurred in any event. AT&T and the Regional Companies shall, jointly or severally, submit to the Court prior to January 1, 1984, the accounting method that will be appropriate for isolating these expenses and for determining whether and when the costs of equal access and of network configuring have been recovered.

the assistance of the Department of Justice and the Federal Communications Commission, whether all costs have been recovered.[38]

## II

## Contingent Liabilities

Under the plan of reorganization, the contingent liabilities of the Bell System are apportioned among AT&T and the Operating Companies on the basis of their relative net investment[39] as of the date of divestiture.[40] Section VIII(H) of the decree allocates to each Operating Company a proportionate share of the System's consolidated debt and equity; and the plan of reorganization provides that the post-divestiture entities will share in the contingent liabilities on the same basis.[41]

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[38] This mechanism has several advantages: it avoids any direct financing partnership between AT&T and the Operating Companies; it requires relatively little monitoring; it gives effect to the access charge tool; it encourages AT&T to work for suitable separations procedures; and it minimizes interference with regulatory commissions.

[39] Contingent liabilities are liabilities which are attributable to pre-divestiture events but do not become certain, and are therefore not booked, until after divestiture. The plan of reorganization defines "net investment" as total assets less reserves for depreciation. AT&T states that it will receive 25 percent of the net investment of the Bell System, and the remaining 75 percent will be assigned to the Operating Companies. AT&T Memorandum, May 23, 1983, at 13 n.*.

[40] The plan provides special allocation rules for contingent liabilities relating exclusively to interstate or intrastate operations or to tax liabilities. See Plan of Reorganization at 188-89. These special rules have either not been specifically challenged by the intervenors, or they have been opposed for the same reasons discussed *infra* for challenging the general rule for allocating contingent liabilities. See, *e.g.*, NASUCA Memorandum, May 25, 1983, at 10.

[41] Under the plan, AT&T and the Operating Companies will be responsible for the payment of judgments and determinations of liability, regardless whether or not an entity was dismissed from the proceeding by virtue of settlement or otherwise. Plan of Reorganization at 190.

The intervenors acquiesce in most aspects of the plan's allocation of contingent liabilities,[42] and they limit their objections in the main to the allocation of contingent antitrust liabilities. Several intervenors assert broadly that because the Operating Companies were not responsible for AT&T's alleged conduct in violation of the antitrust laws and reaped no benefits from such violations, they should not have to share in the liabilities resulting from any antitrust claims. Others make similar arguments more narrowly with respect only to certain types of antitrust violations, such as those relating to the provision of interexchange services or of customer premises equipment (CPE).[43]

The contingent liability provisions of the plan assume (1) that prior to divestiture the Bell System operated as a single unit, and (2) that the residual risks of the System's pre-divestiture operations should be shared by all entities which receive a part of the System's assets. Several intervenors challenge these assumptions.

A. Principle of the Division of the Contingent Liabilities

It is argued by a number of opponents of the plan that for many purposes the Bell System did not operate as a single enterprise. Thus, it is claimed that various Operating Companies charged different rates, operated under different tariffs, were directed by different personnel, and engaged in other practices which differed from company to company. One consequence of this diverse

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[42] No objections were raised with respect to the contingent liabilities having to do with the Bell System's rates, contracts, torts, or taxes.

[43] CPE is used on subscribers' premises to originate, route, or terminate telecommunications (*e.g.*, telephone sets, answering machines). Section IV(E) of the decree.

pattern, according to the plan's opponents, is that some Operating Companies were charged with violations of the antitrust laws along with AT&T while others were not. Further, since under the law a corporation is not automatically liable for the antitrust violations of its affiliates,[44] there is no basis, it is said, for imposing liability upon entities (*i.e.*, the Operating Companies) which have not been or may not be found to have been at fault. Finally, citing *Texas Industries, Inc.* v. *Radcliff Materials, Inc.*, 451 U.S. 630 (1981), several intervenors argue that the plan violates the "rule" against contribution for antitrust damages.[45]

All of these arguments miss the mark. Until the time the reorganization takes effect, the Bell System is legally a single enterprise, with a single claim to the System's assets and a single responsibility for the System's liabilities. It is erroneous, therefore, to pose the problem in terms of imposing liability upon parts of the enterprise based upon fault or lack of fault; at the time the acts complained of occurred there was only one entity (the Bell System), and should there be a judgment in any particular case, that entity will have been found to be at fault.

The evidence at the trial of this case did not isolate specifically whether the fault for particular activities which allegedly violated the antitrust laws lay with personnel assigned to AT&T headquarters or with personnel working for an Operating Company; and, of course, there was no adjudicated final judgment by which such fault could have been parceled out. In view of the commingling and transfers of personnel between AT&T's central

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[44] See, *e.g.*, *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100 (1969).

[45] See, *e.g.*, Comments of Southern Pacific Communications Co., May 23, 1983, at 15; Comments of MCI Communications Corp., May 23, 1983, at 9.

divisions (*e.g.*, Western Electric) and the Operating Companies, it may be that no such decision could ever have been made.[46]

This basic problem with the theory advanced by the intervenors is not cured by the circumstances that some Operating Companies are defendants in some of the pending private antitrust lawsuits while others are not. The decisions of antitrust plaintiffs as to which Operating Companies, if any, should be named as defendants in the private suits appear to have most often been dictated by such non-substantive matters as jurisdiction, venue, and ease of discovery.[47] Such choices were available to the plaintiffs in the various actions because they knew that the cost of any judgment would be shared by AT&T and all Operating Companies[48] regardless whether or not a particular Operating Company was a party to the proceeding in which liability was determined. In short, the identity of the particular Bell defendants played no real substantive part in pre-divestiture lawsuits or judgments, and it would make no sense to regard it as the determinative factor with respect to the payment of judgments based on pre-divestiture conduct which are entered or become final after divestiture actually occurs.

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[46] Because of the integrated nature of the Bell System, it is unlikely that the result would be any different in the private cases brought against that System or its components. In any event, as developed below, it is appropriate to assign the responsibility for the payment of possible judgments now, rather than to leave the issue for resolution for later, on a case-by-case basis. Recognizing this reality, few of the intervenors suggest that the matter be left open until judgments are entered; they argue instead for a fixing of liability now, albeit on a basis different than that assigned by the plan. See pp. 26-28 *infra*.

[47] AT&T Reply Memorandum, May 31, 1983, at 18 n.*.

[48] Such sharing would have occurred through the division of revenues process and a general contribution to the expenses of AT&T's General Department, and it is that Department which would have paid any antitrust judgment irrespective of the Bell entity upon which it might have been imposed. *Id.*; AT&T Response to Objections at 333.

More broadly, it is incorrect to view the plan's allocation of contingent liabilities as an attempt to impose upon this Court the responsibility for making findings concerning fault or for imposing liability with respect to lawsuits pending in other forums.[49] The plan of reorganization does not purport to assign fault; all that is involved here is that, as part of its review of the decree and of the plan of reorganization of the Bell System, the Court has been presented with a proposed contractual arrangement[50] whereby the Operating Companies and AT&T will share in the payment of liabilities arising from pre-divestiture operations regardless of fault—in effect a form of self-insurance. See p. 220 *infra*.

The intervenors' reliance upon *Texas Industries, Inc.* v. *Radcliff Materials, Inc.*, *supra*, as an obstacle to this procedure is misplaced. In that case the Supreme Court held merely that there is no *right* to contribution in antitrust cases;[51] it did not decide, nor was its decision based on

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[49] See, *e.g.*, Satellite Business Systems Memorandum, May 23, 1983, at 4.

[50] The plan provides that in December 1983, the Operating Companies and AT&T will enter into an agreement which will identify all then-pending litigation or other proceedings in which a judgment could result in liability to be allocated under the plan. This agreement will identify whether each contingent liability will be shared by AT&T and the Operating Companies under the net-investment formula or whether it will be treated under one of the special allocation rules. Within one month of the institution of any other action or proceeding against AT&T or an Operating Company based on pre-divestiture events, notice must be given to each entity which may be responsible for payments under the plan. Plan of Reorganization at 189-90, 470.

[51] In that case, the defendant corporation had attempted to file a third-party complaint against other companies seeking contribution should it be held liable under the initial complaint. The Supreme Court upheld the lower court's dismissal of the third-party complaint.

the premise, that contribution is contrary to the policies underlying the antitrust laws.[52] *Texas Instruments* thus does not invalidate either the liability sharing arrangement which presently exists (and has long existed) among the Bell System's components for that System's liabilities or the contractual arrangement proposed for the future by the plan of reorganization.[53]

B. Method of Apportionment

The plan of reorganization proceeds on the basis that the residual risks of the Bell System's pre-divestiture operations should be shared by the entities of the System on the same basis as their receipt of the System's assets and equity.[54] This method of apportion-

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[52] To the contrary, the Court concluded that it was for the Congress, not the courts, to decide whether there should be a statutory right to contribution in antitrust cases and how such contribution should be structured. 451 U.S. at 646.

[53] Arguing that the agreement between the Operating Companies and AT&T to share contingent liabilities should be deemed void as contrary to public policy, one intervenor cites *St. Paul Insurance Companies* v. *Talledega Nursing Home, Inc.*, 606 F.2d 631 (5th Cir. 1979). See Southern Pacific Memorandum of May 23, 1983, at 16. The *St. Paul* decision stands only for the proposition that under Alabama law insurance contracts protecting against intentional wrongs are invalid. Not only are such contracts not universally considered void, but any public policy problems from such contracts are avoided here because the agreement among the Bell companies does not relate to future conduct but applies only to liabilities from pre-divestiture events.

*Zenith* (note 44 *supra*) is likewise inapplicable because the jurisdictional problems there involved are not present here and because of the contractual agreements discussed *infra*.

[54] On this basis, since AT&T will receive 25 percent of the net investment of the Bell System, it will be responsible for 25 percent of the contingent liabilities. See note 39 *supra*.

ment is challenged by several intervenors who suggest a division of contingent liabilities based on a "benefit" or "line of business" approach rather than the "relative net investment" approach provided for by the plan.[55] While this suggestion appears abstractly to have some merit, it is faulty if only because it suffers from serious, indeed insuperable, difficulties in administration.

It may well be doubtful that the Operating Companies benefitted quite as much from the activities challenged in the various pending antitrust suits as AT&T now claims; but it would also surely be incorrect to say that the Operating Companies' past and future lines of business received no benefits. For example, activities which adversely affected competitors of AT&T in the CPE business probably benefitted not only AT&T "headquarters" but also the Operating Companies' own CPE business, and the effects of these activities may even linger so as to continue to provide the local companies with a benefit after divestiture. Further, evidence at the trial of this case indicated significant involvement of the Operating Company personnel in the so-called "procurement" portion of the case, *i.e.*, that dealing, among other things, with CPE.

Likewise, because the Operating Companies received a substantial portion of revenues from interexchange services through the division of revenues process, and because it appears that they stood to lose revenues to the extent that long distance traffic was handled by one

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[55] These intervenors assert (1) that AT&T's future lines of business, not those of the Operating Companies, benefitted from whatever anticompetitive conduct occurred, (2) that the potential liability from alleged anticompetitive conduct bears no necessary relationship to the assets being divided, and (3) that the method prescribed by the plan, coincidentally or otherwise, favors AT&T's interest as against that of the Operating Companies.

of AT&T's competitors, it is difficult to say that they did not benefit from Bell System activities claimed to be unlawful which affected the interexchange market.

For these reasons, several intervenors candidly acknowledge that it is not possible, at least not without lengthy proceedings, to conclude that the Operating Companies received no benefit from the conduct challenged in pending antitrust actions[56] or precisely how such benefits might be allocated between them and AT&T.[57] The Court will go further. In its view, to attempt to trace benefits from conduct challenged in lawsuits not yet decided to lines of business[58] which will be engaged in at a later time by entities which do not yet exist would involve the Court in an impossible, almost metaphysical task, and it is one which, for that reason, it will not undertake.

More affirmatively, the assumption underlying the plan's allocation of contingent liabilities that, as a matter of equity, the contingent liabilities should be shared pro-

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[56] See United Church of Christ Reply, May 31, 1983, at 8 (not possible to determine the extent to which Operating Companies and their ratepayers benefitted from AT&T's policies); General Dynamics Telephone System Center, Inc. Response, May 20, 1983, at 8 (alleged antitrust violations did not necessarily inure to the benefit of the Operating Companies "to the same degree" as they did to AT&T).

[57] Because of this problem, California suggests that the test for allocating contingent liabilities should be: which line of business "primarily" stood to benefit from the antitrust violation? State of California Memorandum, May 25, 1983, at 19. New Mexico advocates that where ultimately there remains a dispute about which entity receives the post-divestiture benefit, the Matter should be submitted to arbitration. State of New Mexico Reply Comments, April 13, 1983, at 5.

[58] The break-up of the Bell System does not, in a number of respects, involve a neat division of operations and lines of business. For example, the Operating Companies will handle some intercity toll calls—especially in some of the larger LATAs—and they will also be able to market CPE.

portionately by all entities which "succeed" to the assets of the Bell System, is not unreasonable. Under the current division of revenues and costs within the Bell System, antitrust liabilities are liabilities of the entire System. Contingent antitrust liabilities—just as the other contingent liabilities not challenged by the intervenors—do not encumber particular assets or particular lines of business; they encumber all of the System's assets and equity. Because the decree provides that the Operating Companies and AT&T will each receive a portion of the consolidated debt and equity of the Bell System,[59] it is reasonable for each of the post-divestiture entities also to receive a corresponding portion of the System's pre-divestiture business risks which encumber the equity.[60]

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[59] The decree provides that AT&T is to divest the Operating Companies with 45 percent debt ratios (55 percent equity). This ratio represents the 1981 (year end) consolidated debt ratio of the Bell System and was also the System's target debt ratio for the end of 1983. See AT&T Reply Comments, June 29, 1982, at 95-96.

[60] The equity portion of the Bell System's capital structure represents, in effect, the shareholders' reserve against business risks, including contingent liabilities. The possibility that certain contingent liabilities may not become certain or may not be turned into debt does not mean that these contingent liabilities are not business risks which currently encumber equity.

One intervenor (Washington Utilities and Transportation Commission Memorandum, May 25, 1983, at 5) argues that, if the Operating Companies were not assigned any contingent liabilities, they could be considered as receiving too much equity only if all other business risks in the overall Bell System capital structure were equal, and it goes on to state that there is good reason to believe that the Operating Companies will face higher risks because they are removed from certain lines of business by the decree. This argument is too speculative. Even though AT&T will retain some of what have been the more lucrative lines of business in the past, these are the competitive lines of business, and there are some who regard them as riskier than the Operating Companies' monopoly exchange functions. See Fortune, *Breaking Up The Phone Company*, June 27, 1983, at 81-91.

The proof of that proposition lies in an examination of the alternatives. If AT&T had decided to settle, insure, or self-insure all contingent liabilities prior to divestiture, the costs of these liabilities would have been reflected now in the Bell System's debt and equity accounts,[61] and

[61] AT&T could have decided to handle the contingent liabilities problem by one of the following methods, all of which would have led to results similar to the apportionment provided for by the plan of reorganization:

(1) The Bell System could have chosen to pay these liabilities through settlement of the litigation before the decree was entered (or before divestiture occurred), such payment to be funded by debt. The Operating Companies would then be divested with higher debt ratios (perhaps 50 percent) to reflect the higher debt ratio of the Bell System. There would then, of course, be no residual risks to divide.

(2) The Bell System could have purchased insurance, with the premiums funded by debt. Again, this would have pushed the System's debt ratio closer to 50 percent, and the allocation of contingent liabilities would then have become irrelevant since any judgment would have been paid by the insurer.

(3) The Bell System could have self-insured the contingent liabilities with a funded reserve of some $25 billion, which would have been borrowed and held in a separate account. The System's debt ratio would again have risen closer to 50 percent, and whichever entity would have been assigned the contingent liabilities would have received this separate reserve account.

(4) The Bell System could have self-insured by booking the contingent liabilities through transfer of a portion of its equity to an appropriate liability account. The choice then would have been either for AT&T to take all the contingent liabilities and the liability account, or AT&T and the Operating Companies each could have taken a share of both the contingent liabilities and the corresponding liability account.

In essence, AT&T and the Operating Companies decided to select the last option—each will receive a share of the contingent liabilities and each will receive more equity than it would have had if one of the other three options had been selected. The only substantive difference between that option and the proposed plan is that the shareholders' equity reserve is not being segregated into a separate liability account. By accepting a share of the contingent liabilities and a higher equity ratio, the Operating Companies are all simply participating in underwriting the System's contingent liabilities. In this way, they are insuring each other, and they will retain any profit which otherwise would have gone to an insurer.

there would have been no need for making provision in the plan of reorganization for the allocation of contingent liabilities. These other options were apparently considered by AT&T and the Operating Companies,[62] and the choice was made that each Operating Company would take on a portion of the System's consolidated equity as well as all associated business risks. In furtherance of that decision, all Bell System Companies are, in essence, insuring one another against the possibility that the contingent liabilities will become certain after divestiture. The chief executives of the Regional Companies have informed the Court that, with but one exception, they agree with the choice made in the plan for allocating the contingent liabilities.[63]

For these reasons, the Court rejects the objections to the treatment accorded in the plan of reorganization to the contingent liabilities,[64] and it will approve that portion of the plan as part of its overall disposition of the parties' motions.

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[62] AT&T Memorandum, May 23, 1983, at 11-12.

[63] See testimony of Thomas Bolger, June 2, 1983, transcript at 25603-04; testimony of William Weiss, June 2, 1983, transcript at 25493-94; but see testimony of Zane Barnes, June 2, 1983, transcript at 25487.

The Court notes that it is entirely unlikely that the contingent liabilities could realistically threaten the viability of the Operating Companies. AT&T has suggested that $25 billion in additional liabilities might become certain after divestiture, but it has since hastened to concede that this possibility is extremely remote. Even if this outside contingency came to pass, the Operating Companies could finance their shares with debt, and their debt ratios would then increase from 45 percent to the 50 percent range—still the typical debt ratio of independent telephone companies and electrical utilities.

[64] The Court has also considered the various provisions made in the plan of reorganization with respect to other liabilities, reserves, and equity, including tax reserves, depreciation reserves, and long term debt, and finds the treatment of these matters in the plan to be reasonable.

## III

### Bell Name and Logo

The plan of reorganization originally submitted by AT&T provided that upon the divestiture both AT&T and the Operating Companies could continue to use the "Bell" name.[65] Complex provisions were made with respect to the Bell trademarks,[66] and the plan further provided that if, in light of the Justice Department's op-

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It is appropriate briefly to mention the debt of Pacific Telephone and Telegraph Co., which has been the subject of several submissions both by the Operating Company and by the State of California. Upon consideration of all the documents, the Court has concluded that it will not require a modification of the plan of reorganization with regard to this issue because the plan is not the appropriate vehicle for determining the extent to which the local company's debt problems may have been created by the California regulators—as was previously assumed by this Court (552 F. Supp. at 208) as well as by the FCC staff (Staff Analysis of February 11, 1983, at 27-28) and various financial rating services—or by AT&T.

The debt equalization scheme which is proposed by California would inappropriately result in inter-regional subsidies and create complex problems leading to new and continuing AT&T entanglements with the Operating Companies. In any event, neither the decree nor the plan of reorganization adversely affects Pacific's financial condition; if anything, they improve it. See Second Supplemental Statement of Donald Guinn, April 7, 1983, at 1. Pacific's interest coverage ratio will be above the level necessary to maintain a Standard & Poor's "A" rating. Supplemental Statement of Donald Guinn, January 13, 1983, at 2; AT&T Response to Objections at 300-01. While future developments and perceptions cannot be vouchsafed, it appears that Pacific will be divested in as financially a sound condition as its prior history permits.

[65] AT&T and the Operating Companies could not use "common corporate names," however.

[66] The Central Staff Organization to be established by the Operating Companies (see Part VIII *infra*) was to receive the rights to the existing Bell trademarks for use in connection with lawful Operating Company business except for the marketing of "equipment not supplied by AT&T and its affiliates." The trademarks include not only the encircled bell logo but also the blue and ochre stripes, and other trademarks and service marks used on vehicles, telephone directories, and the like. They will generally be collectively referred to as the Bell "logo."

position to the AT&T approach, the Court were to disapprove it, AT&T "*will adopt* the alternative . . . [to] retain all uses of the Bell name, including all Bell trademarks, the Bell logo or seal, the blue and ochre stripes, and other graphics and all uses of Bell in corporate names" (emphasis added).[67] The Department of Justice did not oppose the second alternative,[68] but with respect to the first it proposed an amendment which AT&T accepted. It is this Department of Justice version (Amendment No. 15), described in more detail below, which is now before the Court.

Under Amendment No. 15, although the Operating Companies would have exclusive rights to the Bell logo in the United States,[69] they could use it only in connection with the provision of exchange telecommunications services, exchange access services, and printed directory advertising. The Operating Companies would be prohibited from using the Bell logo in connection with the marketing of any customer premises equipment (even that supplied by AT&T and its affiliates). As concerns the "Bell" name, the Operating Companies would be permitted to use it only in connection with services other than the sale of equipment and only when explicitly modified by a geographic designation of an area less than national in scope (*e.g.*, Southwestern Bell); AT&T, on the other hand, could use the name "Bell" on a na-

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[67] If only because of the explicit representations made by AT&T's counsel to the Court during the first Tunney Act hearing in June 1982 (see p. 236 *infra*), this alternative cannot be seriously entertained.

[68] It stipulated, however, that compensation had to be paid to the Operating Companies for the direct costs of revamping their trademarks and trade names.

[69] AT&T would retain its present rights to trade names and trademarks for use outside the United States.

tional basis for all these purposes if preceded by the word "American."[70]

A. Use of the "Bell" Name by both AT&T and the Operating Companies Would Be Confusing

The Department of Justice apparently considered that the original AT&T plan was unacceptable because it could lead to consumer confusion and mutual promotion (*i.e.*, cross subsidization). The proposal presently before the Court is as flawed in those respects as the first plan—if not more so—and it therefore cannot be approved.

There is no question but that the proposal, if implemented, would be confusing as to the relationship between AT&T and the Operating Companies: contrary to fact, it would lead consumers to believe that there is a continuing close connection between these entities or, worse, that they are all still components of the same company. The proposed system—AT&T's use of the "Bell" name preceded by the word "American" and the Operating Companies' use of the "Bell" name preceded by the designation of some smaller geographic area—inevitably suggests that each of the Operating Companies provides service in a particular region of the country while AT&T provides the national service which ties all of the components together into one integrated Bell System. As one of the intervenors correctly points out,

> for AT&T to suggest that consumers will not likely think that 'Illinois Bell' is part of 'American Bell' is

[70] AT&T could continue to use the name "Bell Laboratories" without modification. AT&T could also continue to use the descriptive phrase "Bell System," albeit with the modifier "American." The amendment further provides that AT&T would conduct an extensive advertising campaign to distinguish its products, names, and trademarks from those of the Operating Companies.

> as preposterous as it is that consumers would not think Illinois to be part of America.[71]

This implication, that there is a continuing link between AT&T and the Operating Companies, would have several significant anticompetitive effects: in the market for intercity telecommunications services it would imply that AT&T is the natural or "official" long distance company to be used in conjunction with the local services provided by the several Bell Operating Companies; in the market for consumer premises equipment it would lead consumers to believe that the local system maintained by a "Bell" Operating Company calls for "American Bell" (*i.e.*, AT&T) equipment, or at a minimum, that American Bell equipment is made for and works better than the equipment of other manufacturers when hooked up to the local Bell network;[72] and it would suggest that the local Bell Operating Companies will warrant, service, and repair the equipment of the national Bell company (*i.e.*, AT&T).

It is only to belabor the obvious to record that with respect to each of these areas, AT&T's competitors would, in terms of consumer perception, come off distinctly second best. None of them could claim a similarly close relationship with the local Operating Companies. Sprint and MCI would inevitably be regarded as not as well suited as AT&T to render long distance service in partnership with the local circuits of the Bell Operating Companies; and Tandy and ITT would constantly have

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[71] Reply of Tandy Corporation at 8.

[72] This confusion would exist regardless whether the Operating Companies would market CPE under the Bell label. Even if there were no such marketing, customers would still be led to believe that the providers of local exchange, exchange access, and directory advertising services are intimately connected with American Bell, and that AT&T's equipment—the only equipment that would be marked "Bell"—would be the most adaptable to the local system.

to strive to overcome the perception that, even if their equipment could be connected at all to the local Bell Operating Company loops, it would not operate as smoothly and naturally with them as would AT&T's, and that, again unlike AT&T's equipment, it would not be locally serviced.

The implication of a continuing relationship between AT&T and the Operating Companies is thus inconsistent with the bedrock principles underlying the decree. The principal purpose of the decree was to introduce fair and equitable competition in the telecommunications markets. This was to be achieved by separating the Operating Companies from AT&T so as to ensure that purchasing decisions regarding AT&T's competitive services and equipment would be unaffected by the position of the Operating Companies as the providers of local monopoly exchange and exchange access services.[73] It was, in brief, the decree's purpose to give AT&T's competitors the opportunity to compete with AT&T on equal terms without artificial impediments. The proposal for joint use of the "Bell" name substantially, if not fatally, undercuts these objectives.[74]

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[73] It is on a similar rationale that the Court required modification of the decree to dispel customer confusion arising from joint billing. 552 F. Supp. at 199.

[74] One of the intervenors provided the apt example of a newspaper advertisement proclaiming "NOW YOU CAN BUY GENUINE AMERICAN BELL EQUIPMENT THROUGH THE RETAIL OUTLETS OPERATED BY YOUR LOCAL BELL TELEPHONE COMPANY." Reply of Tandy Corporation at 5. There can be no doubt that consumers would be led to conclude by such an advertisement that these various "Bell" entities are all part of one giant company, and that their equipment was so designed that it would all mesh better than would some other, "foreign" equipment. This would be so if the Bell System had not become fixed in the national consciousness for a hundred years as a single corporation; it is even more true because of that historical fact.

Moreover, as long as AT&T and the Operating Companies both used the "Bell" name, there would also be subsidization between them to the detriment of the other existing and potential competitors. Any promotional efforts by either AT&T or an individual Operating Company would accrue to the benefit of the other, transmitting overtly or subliminally the message that Bell is a single, dominant supplier of telecommunications services and equipment. When an Operating Company advertised under the "Bell" name, it would necessarily also promote the products and services of AT&T marketed under the "American Bell" label, and vice versa. The long-standing consumer association of the "Bell" name with all aspects of the Bell System's local, long distance, and equipment operations would not only persist; it would actually be reinforced.[75]

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[75] AT&T argues, citing several trademark decisions (*e.g., Gould Engineering Co.* v. *Goebel*, 68 N.E.2d 702 (Mass. 1946); *Gemeinde Bran, Inc.* v. *Amana Society*, 557 F.2d 638 (8th Cir. 1977)) that different businesses which "share a common heritage" may use the same mark in separable parts of the business. See Response to Comments at 480-90. That argument lacks merit. Trademark law as it has developed in the context of claims of unfair competition between competing concerns is of dubious applicability to a situation—divestiture under antitrust principles—where the interests of outside competitors and the public are implicated. *Cf. Ford Motor Co.* v. *United States*, 405 U.S. 562, 576 & n.11 (1971). In any event, the lines of businesses of AT&T and the Operating Companies are not separable but related and, in the equipment market, they will be direct competitors. The customer confusion this would foster would delay achievement of a truly competitive CPE industry.

It was for similar reasons that the various oil companies which emerged from the 1911 break-up of Standard Oil have generally been prohibited from doing business under a Standard Oil name or trademark in a territory where Standard Oil denoted another product. See, *e.g., Standard Oil Co. (Kentucky)* v. *Humble Oil & Refining Co.*, 363 F.2d 945, 951 (5th Cir. 1966) ("we think long cumbersome records are no longer necessary to prove the public believes that all of the pseudonyms for Standard Oil belong to the same or related companies").

The decree is designed to effect a radical separation of the Operating Companies from AT&T;[76] it will hardly do to continue to have the various divested entities of the Bell System[77] hold themselves out as if they were all still part of the same complex.[78] The plan proposed by AT&T would create the impression to the consuming public that the divestiture had never taken place. The Court did not approve a decree breaking up the Bell System to have that system rise again, phoenix-like, in the plan of reorganization.

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[76] The various components of the Bell System will, to be sure, be separated from each other in a legal, ownership, and financial sense. But if they were all to support each other in their marketing and promotional efforts, not a great deal will have been gained. Together they would still crowd out all others; together they would still be the colossus of telecommunications.

[77] Use by AT&T of the terms "Bell System" or "American Bell System" is particularly troublesome, for it implies that the system that will be broken up on January 1, 1984 actually survives in the form of AT&T.

[78] It is worth noting also that this confusion is actually being encouraged by AT&T's current advertising which features such phrases as "Bell System" and "Genuine Bell." Indeed, AT&T announced its decision to name its equipment marketing subsidiary "American Bell, Inc." after it had learned of the Department of Justice's objection to the use by AT&T of the word "Bell" in any way which could imply a continuing "endorsement or relationship between the BOCs' monopoly local exchange service and the products and services of AT&T and its affiliates" (letter of September 23, 1982, from William F. Baxter to Howard J. Trienens (Exhibit D to Objections of Tandy Corp., filed February 18, 1983)) and after at least one intervenor in the public interest proceeding before this Court (Tandy Corp.) had similarly complained about such use. AT&T advertising focusing on the word "Bell" has proceeded at a crescendo since the divestiture decision was made.

Because of this history, not much faith can be placed in AT&T's promise to undertake an advertising campaign to educate consumers as to the differences between the new entities. An effective campaign along these lines would be directly contrary to AT&T's interests.

For these reasons, the "Bell" name and the Bell logo must belong either to AT&T or to the Operating Companies—but not to both.

B. AT&T Is Not Entitled to the "Bell" Name and Logo as a Matter of Right

Since the concurrent use by AT&T and the Operating Companies of the name "Bell" cannot be approved, it remains to be decided which entity or entities should inherit that name—and along with it the logo—as part of the divestiture. Before proceeding to determine whether AT&T or the Operating Companies should, consistently with the decree's principles, be assigned the Bell tradename and trademark, consideration must be given to several preliminary arguments made by AT&T.

First. AT&T contends that it owns the "Bell" name,[79] from which it would presumably follow that it cannot be deprived thereof without its acquiescence. That argument is not well taken.

All of the assets of the combined Bell System are the property of AT&T[80] yet some—indeed the majority—of these assets are being assigned by the decree to the Operating Companies. If AT&T had a veto power stemming from general principles of property law with respect to the "Bell" name, it would have the same kind of power with regard to all other Bell System assets. Obviously that is not so, in the context of a distribution of assets and liabilities stemming from a break-up of the

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[79] Plan of Reorganization at 415.

[80] See 552 F. Supp. at 201-04.

corporation under a court-approved decree.[81] The question actually is a much more simple and direct one: how should the assets represented by the "Bell" name and logo be distributed in order to effectuate the provisions and principles of the decree—an issue which is considered in Part C below.

Second. AT&T next claims that the "Bell" name is part of the heritage of AT&T,[82] and that customers who have purchased Bell telephones and services and who may want to patronize Bell System companies in the future are entitled to know, post-divestiture, which companies "are historically related to those products and services they have enjoyed for a hundred years."

But not only is that name as much a part of the heritage of the Bell Operating Companies as that of AT&T, but, in the public mind, "Bell" may well be said to stand primarily for the local companies, for that is where the public has traditionally obtained its telephones and its service.[83] It was the Operating Company to which one turned with a malfunction, a complaint, a request for new or altered service, a billing inquiry, and the like. The function of a trademark or tradename is to indicate the

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[81] See *Ford Motor Co.* v. *United States*, *supra*, 405 U.S. at 576 and n.11. AT&T also "owns" a sizable magnitude of liabilities, including the contingent liabilities the responsibility for which will pass in large part to the Operating Companies (see Part II *supra*), yet it has never taken the position with respect to these liabilities that they constitute its obligation as distinguished from that of the Operating Companies.

[82] The reference to a "common heritage" is puzzling for another reason as well. It is because that common heritage was allegedly used to violate the antitrust laws, and it is presumably because the "common heritage" was so intrinsically anticompetitive, defying less drastic remedies such as injunctions, that this lawsuit was filed and this divestiture agreement was made and approved.

[83] Response to Objections at 486-87.

party which "puts the goods on the market and accepts the responsibility or plaudits for their acceptability or quality." E. Vandenburgh, Trademark Law and Procedure at 34 (2d ed. & 1979 Supplement).[84] In this instance, that means, more than any other entity, the Operating Companies.

Third. AT&T contends that the name "Bell" is assigned to it by the plan of reorganization and that this assignment should not be disturbed because it allegedly is not inconsistent with the provisions of the decree. It is true that the Department of Justice has capitulated to this argument, stating that it could find no basis for

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[84] AT&T also claims that the trademark and the tradename Bell belongs to the party which manufactured Bell equipment, *i.e.*, Western Electric Co. However, as one commentator put it,

> When one says that a trademark must indicate origin of the goods to which it is applied, it is not intended to [imply] that a trademark can only be used by a manufacturer of the goods. . . . The origin to which reference is made is the party that introduces the goods on which the mark is used into commerce with the trademark on them and who primarily stands to gain or lose by the acceptable qualities of the goods. It is not even necessary that the public or purchasers know who is the manufacturer of the goods . . . .

E. Vandenburgh, Trademark Law and Procedure at 35 (2d ed).

Moreover, it is undisputed that AT&T has not supplied to the Operating Companies and hence held out to the public only products made by it or its affiliates. See Amended Certification of Thomas E. Bolger, April 6, 1983, at 4.

While certainly a survey of the public would indicate that the name "Bell" and the Bell logo do not connote the same thing to every single person—an individual who has written checks monthly to one of the Operating Companies which does not use the name "Bell" in its corporate name may be more likely to think of "Ma Bell" than of a local Operating Company, for instance—it cannot be gainsaid that the primary connection between the individual and the Bell System occurred between telephone subscriber and local Operating Company. Assignment of Bell name and logo to the Operating Companies is thus consistent with trademark law.

overturning the AT&T decision. But the provisions of the plan drawn by AT&T are entitled to much less weight here than in other circumstances, since it is clear from the submissions of the designated chief executives of the Regional Companies that a number of them oppose the proposed disposition of the Bell name and logo.[85] Beyond that, as the Court has had occasion to explain a number of times, the plan of reorganization, to be approved, must be consistent not only with the provisions of the decree but also with the underlying principles. For the substantive reasons discussed below, an assignment of the "Bell" name and logo, or either, to AT&T would not be consistent with these principles.

C. Use of the Bell Name and Logo Are More Appropriately Assigned to the Operating Companies than to AT&T

Both the original plan and the proposed Department of Justice amendment would deny to the Operating Companies the use of the Bell name and logo in marketing customer premises equipment (CPE).[86] The former would have severely limited this use; the latter would preclude it altogether. It is this aspect which has drawn the widest criticism—from the States, the interexchange carriers, the manufacturers of CPE, and the Operating Companies themselves. In the view of the Court, the critics are entirely correct.

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[85] See, *e.g.*, Statement of Wallace R. Bunn, May 23, 1983; Reply Memorandum of the Midwest Regional Holding Co., May 31, 1983; Supplemental Statement of Zane E. Barnes, April 12, 1983. Here, again, AT&T cannot have it both ways: it cannot relegate the largest share of the Bell System obligations to the Operating Companies yet purport to speak conclusively on behalf of the entire System with regard to the plan of reorganization even where there is a sharp dispute among the various components. See note 81 *supra*.

[86] See note 43 *supra*.

The decree as ultimately entered expressly authorized the Operating Companies to market customer premises equipment. The Court fully explained why it required this modification as a condition of its approval of the decree:

> As against [the] relatively slight risks to competition from Operating Company involvement in the marketing of CPE must be weighed the very substantial contribution these companies could make to vigorous competition in the customer premises equipment market. . . . The Operating Companies, with their existing relationship to telephone users, are more likely than any other competitive entity to provide an effective counter-balance to AT&T's market strength and thereby to promote a genuinely competitive market.

552 F. Supp. at 192 (footnotes omitted).[47]

To deprive the Operating Companies of the use of the Bell logo and the Bell name in the CPE area would effectively cripple their efforts to become viable competitors in this market. The Court approved the decree in the expectation that the Operating Companies would be able to use their "existing relationship to telephone subscribers"

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[47] The Court repeated this reasoning in its Memorandum of August 23, 1982, denying the Justice Department's motion for reconsideration (at p. 5):

> Balanced against the remote contingency that the Operating Companies would engage in anticompetitive conduct is the certainty that they would provide healthy competition for AT&T. . . . Allowing the Operating Companies to engage in providing CPE will serve as a useful competitive check on AT&T, not only deterring the possibility of anticompetitive behavior but also benefitting consumers by increasing the number of equipment providers in the market place.

in marketing equipment as a counter to AT&T's market strength.[88]

The various Operating Company officials who provided comments to the Court[89] on this aspect of the plan of reorganization attested to the fact that their

> principal strength in the marketplace for customer premises equipment (and other potential services which may be approved by the Court) [is their] long and solid reputation for quality products and excellent service. Our ability to trade on that hard earned reputation is important and should not be compromised by denying us the ability to use the Bell logo and marks as legitimate reminders of who we are.[90]

Several executives of the new Regional Companies have stated that they might have to stay out of the equipment market entirely (or limit themselves to the sale of large-scale equipment) if they were prevented from using the Bell name and logo in connection with equipment marketing. See testimony of Thomas Bolger, June 2, 1983, transcript at 25601-02; see also, Wall Street Journal, *Some Bell Companies May Stop Supplying Residential Phones as Competition Grows*, June 17, 1983.

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[88] August 23, 1982, Memorandum Opinion at 4 n.7. Since the provision allowing the marketing of CPE was added to the decree at the Court's insistence, it would not be unreasonable to regard the Court's expectations in that regard as the most accurate expression of the decree's "intent."

[89] A substantial amount of testimony at the June 2, 1983, hearing was devoted to this issue.

[90] Letter dated April 13, 1983, from Raymond F. Burke, Vice President and General Counsel-designate of the the Northeast region; see also, *e.g.*, Supplement to Sworn Statement of Wallace R. Bunn, chief executive officer-designate of Southeast region; Statement of Thomas Bolger at 2-3.

It would not be similarly inimical to the purposes and principles of the decree to preclude AT&T from the use of the Bell name and logo. One principle underlying the decree is that both AT&T and the Operating Companies shall be in a position to be vigorous competitors with each other and with others in the marketing of customer premises equipment. To that end, the decree sets up a carefully balanced structure, as follows. AT&T will retain all embedded CPE; it will retain the Bell System retail outlets; and it will retain the ability both to manufacture and to market CPE. The decree further took into account in this regard that, by comparison with the individual Operating Companies, AT&T will be a giant, with financial and other resources far overshadowing those of the local entities.

The Operating Companies, on the other hand, will come out of the divestiture with relatively limited CPE-related resources and functions. They will be prohibited from manufacturing CPE; they will be deprived in part of their existing customer base by the assignment of existing CPE to AT&T; they will lack the ready-made outlet of existing retail stores; and they will not have the benefit of Bell personnel experienced in the marketing of CPE. Insofar as such marketing is concerned, these companies will essentially be limited to their proximity to the local customer base in addition to the goodwill inherent in the "Bell" name and logo (if these are assigned to them). In short, in competitive terms, the assignment of the Bell name and logo to the Operating Companies rather than to AT&T can hardly be characterized as unfair to the latter.[91] The true situation is that, without the name and logo the local companies' right, under the

[91] There is some merit to AT&T's point that its employees have an emotional attachment to the Bell name, and that to them the name's passing may mean the loss of an emblem of pride and perhaps lifelong association. The same could be said about employees of the Operating Companies, however.

decree, to market CPE would be defeated, while AT&T's right to do so would only be minimally affected.[22]

It is appropriate, finally, to quote from the representations which were made to the Court by AT&T's counsel at last year's public interest hearing. On June 29, 1982, counsel stated in response to comments made by an attorney representing a competitor that

> . . . The problem is not the logo, the yellow and blue stripes and that sort of thing. . . . We do not want to get into that fight and we have already agreed . . . that the Bell that you know, the stripes that you have come to know they will go to the BOCs. Trucks that get repainted will be the Long Lines trucks, [not?] the BOC trucks.
>
> The only thing left then is the names. I think Tandy's counsel was very appropriate in saying that after all, you're breaking up the Bell System. . . . What he objected to was concurrent use of the same corporate names. I stand before you and say there will be no such concurrent use of the same corporate name after the split.

When the Court suggested that this understanding had best be incorporated in the decree, AT&T's counsel replied that this was not necessary because

> [t]he question has been raised about these common names, the Court Reporter is recording this and there is a record of this hearing that should well outlast all of us, I suppose.

Transcript at 25214-15.

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[22] It is significant also, in antitrust terms, that transfer of the Bell name and logo to the Operating Companies will not eliminate AT&T as a competitor but will yield two competitors where otherwise there might only be one. *Cf. United States* v. *Lever Brothers Co.*, 216 F. Supp. 887 (S.D.N.Y. 1963).

To be sure, it could be argued that these statements are not without some ambiguity.[93] Yet the overwhelming sense of the representation, particularly when juxtaposed against the arguments made by counsel for one of AT&T's competitors and that of the Department of Justice, was that AT&T was content to have the Operating Companies inherit the Bell logo and name.[94]

For the reasons stated, the Court will refuse to approve the plan of reorganization unless it is amended to provide for use of the "Bell" name and logo by the Operating Companies (except as provided in Part D *infra*) and for a prohibition on AT&T's use after January 1, 1984,[95] of the "Bell" name or the word "Bell" in any

[93] AT&T suggests that it is not, even now, proposing "common corporate names." When the promise was made that there would be no "common corporate means," it would have been difficult to visualize that AT&T promised only that a modifier would be added to the word "Bell" but that otherwise that name would still be used by all of the successor entities of the Bell System. Had not AT&T's counsel hastened to assure the Court that no amendment of the proposed decree was necessary, the Court would have, then and there, insisted upon language which is not susceptible of the current "fine print" argument.

[94] The assignment of the Bell name and logo to the Operating Companies rather than to AT&T is further consistent with those provisions of the decree which distribute assets on the basis of predominant use. As the Department of Justice points out,

> [a]ssignment of the Bell logo and marks to AT&T would create relatively more transitional costs, due to the relatively greater number of BOC assets upon which the marks and logo appear, in comparison to those retained by AT&T, *e.g.*, on buildings, trucks, phone booths.

Department of Justice Response to Comments at 155.

[95] The Court will consider postponing the effective date of the prohibition for an additional six months upon a showing by AT&T made by November 1, 1983, that it needs more time to continue a promotional campaign with respect to whatever name it desires to adopt in place of "American Bell." Although to some extent AT&T has created this problem by its recent intensive advertising campaign (see note 78 *supra*), it is nevertheless appropriate to allow it a reasonable period within which to extricate itself from this situation.

existing or new corporate name or in connection with the manufacture or marketing of any product or service, or for any other purpose.[96]

D. Limitations on the Operating Companies

The use which the Operating Companies may make of the Bell name and logo requires additional discussion.

First. Under the current version of the plan of reorganization, the "Bell" trademarks are to be assigned to the Central Staff Organization.[97] However, if the CSO were to receive the assignment of the name and logo, it might also have to administer centrally a program of quality control, for lack of reasonable "quality control" could be regarded as working an abandonment of the licensor's registration of its trademark. See Lanham Act, 15 U.S.C. §1051 *et seq.*; *Dawn Donut Co.* v. *Hart's Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959). Such monitoring of the Operating Companies by the CSO would run counter to the notion that it is the Operating Companies which control the CSO, not vice versa. Moreover, each Regional Company must have individual responsibility for giving meaning to the products or services it offers under the name Bell, consistent with trademark and antitrust law. Accordingly, the Court will require that the tradename and trademarks shall pass directly to the Regional Companies, without intervention of the CSO.

Second. With respect to exchange telecommunications, exchange access, and directory advertising, the

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[96] AT&T may, however, continue to use the "Bell" name with respect to its Bell Laboratories and its foreign operations. The Laboratories and the foreign operations will not be in competition with the Operating Companies, and use of the "Bell" name in these contexts will not otherwise be confusing.

[97] See Part VIII *infra*.

Operating Companies and the Regional Companies will, by definition, be limited to clearly defined geographic areas, and they will therefore use the name "Bell" only in conjunction with a geographic designation indicating the relevant territory. Likewise, in their corporate names, the Operating and Regional Companies will use "Bell" only in conjunction with a geographic prefix. In the marketing of equipment, however, these companies may wish to compete in places beyond their service territories, particularly with respect to the sale of large-scale telecommunications equipment to business customers. There is no reason why such competition should be precluded by the imposition of territorial restrictions.[98]

To the extent that an Operating Company sold CPE within its own geographic area, there might be no problem. Confusion would result, however, if hypothetically, Southern Bell, Northwestern Bell, and Pennsylvania Bell all marketed equipment in, say, Chicago, simply as "Bell" products, or if they stamped only the Bell logo on the equipment they sold there. The name "Bell" would in that case have little meaning; both it and the logo might be of dubious legitimacy under trademark law; and each company would run the risk of being sued by Illinois Bell for unfair competition. Accordingly, an Operating Company wishing to trade in another's territory shall not use the name "Bell" without a trade modifier, nor may it use the logo standing alone. See, *e.g.*, *Standard Oil Company*

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[98] Such restrictions have in other contexts been found to violate the antitrust laws. See, *e.g.*, *Ohio-Sealy Mattress Manufacturing Co.* v. *Sealy, Inc.*, 585 F.2d 821 (7th Cir. 1978).

v. *Standard Oil Company*, 252 F.2d 65 (10th Cir. 1958); *Mister Donut of America, Inc.* v. *Mr. Donut, Inc.*, 418 F.2d 838 (9th Cir. 1969).[99]

## IV

## PATENTS

The issue before the Court is not, as it is with regard to the Bell name and logo, whether the Bell System patents should be assigned to AT&T or to the Operating Companies. AT&T will, in any event, retain ownership of all the patents. The question to be decided is the extent to which the Operating Companies will share in the patents by being granted licenses thereto, and what right these companies should have to grant sublicenses to others.

### A. Meaning of the Decree

The plan of reorganization provides that the Operating Companies will be granted royalty-free licenses to use patents[100] now owned by AT&T or to be issued to AT&T within five years after divestiture, to the extent that they relate to exchange, exchange access, and printed

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[99] Whether use of the word "Bell" with an appropriate prefix could pass muster under the law of trademarks and unfair competition outside a particular Regional Company's territory may be expected to depend upon the particular facts of each use (*e.g.*, the precise configuration of the name and logo, the results of customer surveys, and the like). Any decision now on that issue would therefore not only be entirely speculative and premature but it might also be beyond the Court's jurisdiction, and it will accordingly be left to another day and another forum.

[100] "Patents" as used in this Opinion includes non-patented technical information. The parties have agreed that the Operating Companies would be granted rights not only to patents but also to all technical information funded by the license contracts. 552 F. Supp. at 177. The plan as proposed applies only to United States patents; the Operating Companies would receive no rights to foreign patents. Objections to this aspect of the plan are discussed at note 116 *infra*.

directory advertising services.[101] Under the plan, the Operating Companies will not, however, be granted licenses to patents relating (1) to any services which the decree prohibits them from offering (such as inter-LATA service) and (2) to the provision of customer premises equipment. To justify these limitations, AT&T and the Department of Justice rely upon section I(A)(1) of the decree, which provides, *inter alia*, for the

> transfer from AT&T . . . to the BOCs . . . of sufficient . . . rights to technical information to permit the BOCs to perform, independently of AT&T, exchange telecommunications and exchange access functions

and on section VIII(B) which provides that

> all facilities, personnel, systems, and rights to technical information owned by AT&T . . . which are necessary for the production, publication, and distribution of printed advertising directories shall be transferred to the separated BOCs.

In the view of these parties, no patent rights need to be granted to the Operating Companies on any basis other than these explicit provisions contained within the "four corners" of the decree. This is erroneous.

When the Court approved the proposed decree on August 11, 1982, it made the approval contingent upon the adoption by the parties of a number of modifications.

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[101] AT&T's original proposal, which was modified at the request of the Department of Justice, would not have permitted the Operating Companies to engage in sublicensing on their own at all but would have required them to request AT&T to perform all sublicensing for them. The parties have since agreed to a modification of this part of the plan, and each Operating Company will now have the right directly to sublicense patents to any firm for use in supplying goods or services to that company, regardless whether the sublicensee is then a party to a license agreement with AT&T. See Department of Justice Response to Comments at 141.

These modifications, it was made clear at the time, were required only for the most substantial changes or clarifications; with respect to other subjects, the Court stated that it was content to rely upon the parties' representations and promises and its own authority to give them effect during the implementation proceedings, including by its authority to approve or disapprove of the plan of reorganization. Thus, the August 11, 1982 Opinion explained

> With respect to a number of subjects, the proposed decree establishes merely general principles and objectives, leaving the specific implementing details for subsequent action, principally by the plan of reorganization. . . . *The parties have also made informal promises*, either to each other or to the Court, *as to how they intend to interpret or implement various provisions.* The Court has decided that its public interest responsibilities require that it establish a process for determining *whether the plan of reorganization and other, subsequent actions by AT&T actually implement these principles and promises* in keeping with the objectives of the judgment. . . .
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> For that reason, the Court is requiring that the judgment be modified . . . to provide for a proceeding . . . in which *the Court will determine whether the plan of reorganization is consistent with the decree's general principles and promises* (emphasis added).

552 F. Supp. at 224-25.

One of these promises concerned patents. In its August 11, 1982 Opinion, the Court took note of the fact that

> AT&T has proposed granting to the Operating Companies, on a royalty-free basis, *all* existing patents and all patents issued for a period of five years following approval of the proposed decree.

552 F. Supp. at 177 (emphasis added).[102] This statement was not conjured up by the Court; it reflects repeated representations made to it both by AT&T and by the Department of Justice. For example, the Department stated in its Response to Public Comments of May 20, 1982 at 132 that

> the reorganization plan will require AT&T to grant royalty-free licenses to the BOCs for *all* of its existing patents, and for *all* patents issued for a period of five years following entry of the proposed modification (emphasis added).

See also Department of Justice Response to Public Comments, May 20, 1982, at 38; AT&T Reply to Comments, May 21, 1982, at 123; and see note 105 *infra*.

These various representations, said the Court it its August 11, 1982 Opinion,

> are adequate to support the conclusion that the Operating Companies will possess the necessary patent and technical information resources.[103]

The arguments now made by AT&T and the Department of Justice in support of their claim that the word "all" in their several representations to the Court did not really mean "all," and that in context they meant something else, are disingenuous to say the least.[104]

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[102] The Court further relied on the fact that "the parties have assured the Court that the Operating Companies will have the right to sublicense the AT&T patents and technical information to those providing them with goods and services." 552 F. Supp. at 177.

[103] 552 F. Supp. at 177. Neither AT&T nor the Department of Justice thereafter contradicted the Court's understanding, whether by a motion for reconsideration or otherwise.

[104] Indeed, the Court is disturbed that representations made by both parties in so clear and unequivocal a fashion are now claimed, after the decree has been entered, to be encumbered by gaping loopholes.

Both parties base their narrow interpretations on the circumstance that the representations were made at a time when the proposed decree would have limited the Operating Companies to exchange telecommunications and exchange access services.[105] While this is an accurate depiction of their timing, it does not in the least support the conclusion that the promises were or reasonably should have been regarded as limited to patents which related to these lines of business.

These promises, whatever their timing, were relevant not only to the question of what resources were required to be transferred to the Operating Companies to imple-

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[105] See AT&T May 31, 1983 Memorandum at 24; Department of Justice Memorandum, June 10, 1983, at 3.

The Department of Justice points out that AT&T made the following statement during the Tunney Act proceedings:

> [T]he Decree requires that AT&T afford the BOCs sufficient technical information to independently provide exchange telecommunications service and exchange access functions (Decree, §I(A)(1)). In compliance with that provision, AT&T will continue to license to the BOCs on a royalty-free basis existing patents and patents issuing within five years after entry of the Decree. AT&T Reply Comments, May 21, 1982, at 123.

The Department further referred to its May 20, 1982 Response to Public Comments at 38, where it stated:

> In addition, AT&T has made a commitment to the Department that it will continue to license to the BOCs, on a royalty-free basis, all existing patents and patents issued within five years of the date of entry of the modification. Such licenses will be for the life of the patent and will include the right to grant sublicensee to others to provide the BOCs with goods and services *for the BOCs' own use* (emphasis added).

Department of Justice June 10, 1983 Memorandum at 3.

The Department argues that the "own use" limitation is not consistent with an interpretation that these companies would be granted the right to sublicense patents to manufacturers who provided them with products for resale. But the decree grants to the Operating Companies the right to provide CPE, and these companies obviously need to be supplied with products to use in selling CPE to the general public. See *infra*.

ment the exchange telecommunications and access service provisions of section I(A)(1), but also to two other issues—whether the Operating Companies should receive licenses to patents which they had in substantial part financed, and whether AT&T should be relieved of the obligation, imposed by the 1956 decree, to license its patents to all applicants on a nondiscriminatory basis.

First. There were numerous references throughout the Tunney Act proceedings to the fact that the Operating Companies, by means of the licensing contracts, had contributed substantial amounts to the cost of the research which led to the patents, and this was always regarded by all as at least a possible basis for awarding licenses to the patents to these companies. See, *e.g.*, Department of Justice Response to Public Comments, May 20, 1982, at 38.

Second. The Department of Justice took the position during the Tunney Act proceedings that it was reasonable and in the public interest to relieve AT&T of the patent provisions of the 1956 decree which required it to grant licenses to all comers, foreign and domestic. One basic argument made to buttress the claim of reasonableness was that the fruits of the Bell System research would not simply be lost to the world because the reorganization plan would still require AT&T to grant royalty-free licenses to the Operating Companies for all of its existing patents and for all patents issued for a period of five years following entry of the decree.[106] The Department explained that the effect of such a grant would be that

> the BOCs will have the right to sublicense these patents for their own use, including the manufacture of equipment for the BOCs' purchase. Thus, as a prac-

[106] Department of Justice Response to Public Comments, May 20, 1982, at 132.

> tical matter, many AT&T patents issued within the next several years must also be licensed to AT&T's competitors notwithstanding entry of the proposed modification.
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> . . .
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> Because of the existence of requirements that AT&T license patents heretofore issued or issued during the next five years, and in view of the BOCs' sublicensing rights, it is apparent that a significant portion, if not all, of such 'work in progress' patents will be licensed. . . . [T]here is no reason to believe that entry of the proposed modification will result in the removal of 'work in progress' patents from the pool of AT&T patents generally available to industry.[197]

This expansive description of the proposed distribution of patent rights was not in any way limited, explicitly or implicitly, to section I(A)(1) of the decree or to intra-LATA services. The Justice Department's reference was to the effect of the proposed decree on the mandatory licensing provisions of the 1956 decree—and these provisions clearly applied to all Bell System patents (including, of course, the CPE patents).

There is, in view of that history, no reasonable basis for the conclusion that the various references by AT&T and the Department of Justice to "all" patents did not mean just that, or that CPE patents in particular were meant to be withheld from the Operating Companies. Thus, when the decree was modified to authorize the Operating Companies to provide CPE, there was no need again to specify the patent rights incidental to this

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[197] *Id.* at 132-33.

modification[108]—rights which were already guaranteed to the Operating Companies by the parties' representations and by the Court's retention of jurisdiction to give effect thereto. As the Court said with reference to patents and technical information,

> When [the plan of reorganization] is submitted . . . the Court will evaluate [that plan] to make certain that [the appropriate details] conform to the general principles implied by these assurances.

552 F. Supp. at 177.

AT&T next contends that, if it were required to license all the Bell System patents to the Operating Companies which would then have the right to sublicense these patents to others, it would be required to "give away *its* technology" (emphasis added).[109] That formulation misstates the issue. Because of their financing of much Bell System research through the licensing contracts,

[108] The Department of Justice and AT&T also point out that section VIII(B)—which authorizes the Operating Companies to provide printed directory advertising services (*i.e.*, Yellow Pages)—specifically provides that the technical information necessary to provide such services should be transferred to the Operating Companies. From this premise they argue that since section VIII(A)—which authorizes the Operating Companies to provide CPE—is silent with regard to the transfer of technical information, the conclusion may be drawn that no transfer of CPE patents to the Operating Companies was intended.

This argument is likewise unpersuasive, since there is another, more plausible explanation for the variation between sections VIII(A) and VIII(B). The language in section VIII(B) concerning technical information is part of a larger provision, similar to section I(A)(1), which was intended to result in the transfer to the Operating Companies of all Bell System assets used in the production of printed directories. See 552 F. Supp. at 194 n.263. If this provision had been used in the CPE context, it would have effectively assigned to the Operating Companies the embedded CPE and the existing network of retail outlets, contrary to the Court's intent. See 552 F. Supp. at 192 n.248.

[109] AT&T Response to Objections at 462.

what the Operating Companies will be receiving cannot fairly be described as AT&T's technology;[110] that technology is as much theirs as it is AT&T's. See 552 F. Supp. at 177.[111] Also, as the Court has already noted (see Part II above) all of the assets and all of the liabilities of the Bell System are being distributed between AT&T and the Operating Companies. AT&T cannot assert that, in the context of that distribution, the patents are "its" technology unless it is also prepared to live with the proposition that the liabilities of the Bell System are "its" liabilities. In short, it is entirely appropriate under the decree for the Operating Companies to receive licenses to the existing patents and to those which will be issued within the next five years.[112]

AT&T and the Department of Justice finally argue that under this rule, the Operating Companies would receive licenses to patents for services which the decree currently prohibits them from offering,[113] and that there could be no justification for such an action. It is not true, however, that even with respect to such subjects as inter-LATA services, the Operating Companies will be entirely barred from entry; they will be in these lines of business as of the very date of divestiture, albeit on a

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[110] That is, "central" AT&T, as distinguished from the Bell System as a whole.

[111] This is so even if it is assumed, as AT&T asserts, that no expenses have been billed to the Operating Companies for new CPE patents since May 1980. See testimony of Thomas Bolger, designated chief executive of Mid-Atlantic Region, June 2, 1983, transcript at 25594, 25597-98.

[112] With regard to all patents, AT&T will retain ownership and the right to use them in any lawful way it sees fit. None of the licensing requirements in the decree or in the plan of reorganization as required to be modified by the Court changes that fact in any way.

[113] *E.g.*, patents applicable directly to inter-LATA services or to foreign operations.

limited scale,[114] and they will therefore be able legitimately to make use of the pertinent patents[115] and the technology they represent.[116] Additionally, the line of business restrictions which will initially apply might in the future be lifted by the Court pursuant to section VIII(C) of the decree, and the patents would be useful to the Operating Companies at that time.[117]

B. Sublicensing by the Operating Companies

It is thus clear that, in view of the representations made by the parties and accepted by the Court as part of the decree, as well as in view of the various supporting considerations (*e.g.*, that the Operating Companies in significant part financed the research which produced the patents), the local companies are entitled to licenses to all the patents secured during the course of their association with AT&T and for five years after the association

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[114] *E.g.*, in the so-called "corridors" and the Official Services (see pp. 294 and 273 *infra*).

[115] See, *e.g.*, testimony of Thomas Bolger, June 2, 1983, transcript at 25595.

[116] With regard to foreign patents, AT&T argues that since the Operating Companies' exchange operations are confined to this country, the rights to AT&T's domestic patents provide all the patent rights the Operating Companies require to conduct exchange and directory advertising operations. AT&T Memorandum, May 31, 1983, at 24 n.**. However, in the CPE area, at least, foreign patents could be helpful to the Operating Companies even though they will not be operating overseas, for rights to foreign patents will enable them to purchase CPE which is manufactured entirely or in part by foreign companies. See testimony of Thomas Bolger, June 2, 1983, transcript at 25600; Memorandum of Mid-West Regional Holding Company, May 23, 1983, at 19; Memorandum of Mid-West Regional Holding Company, May 31, 1983, at 8.

[117] The Operating Companies would benefit from these rights if any of the line of business restrictions should be lifted *at any time during the life of the particular patent*, not simply during the five years after divestiture. A lifting of the restrictions, or some of them, during that extended period is certainly conceivable.

is dissolved.[118] This does not mean, however, as AT&T assumes and as some of the intervenors strenuously urge, that the Operating Companies may make direct use of the patents with respect to services which are otherwise forbidden to them by the decree. What must be firmly kept in mind is that, since the Operating Companies will not be allowed to enter manufacturing, they will be able to make effective use of the patent licenses only to the extent that they will have the power to grant sublicenses to manufacturers. As explained below, that power will exist with respect to some subjects immediately upon divestiture; with respect to others it is inchoate and its actual exercise will depend upon the removal of the line of business restrictions under section VIII(C).

The Operating Companies may grant sublicenses consistently with the decree to the extent that they will use the technology covered by the particular patents in their provision of products and services which they are authorized to sell or render.[119] They may not, however,

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[118] It may be noted that requests to modify the proposed plan of reorganization so as to broaden the scope of patent rights granted to the Operating Companies were made by the Midwest Regional Holding Company (see Reply Memorandum of May 31, 1983); Thomas Bolger, designated chief executive of the Mid-Atlantic Region (see Second Amended Certificate of June 10, 1983); and Wallace R. Bunn, designated chief executive of the Southeast Region (see Statement of May 23, 1983).

[119] See 552 F. Supp. at 177 (Operating Companies may grant sublicenses "to those providing them with goods and services"). Likewise, the Plan of Reorganization at 411-12, as modified by Amendment 34, provides that

> AT&T will grant to each BOC the right—which no BOC currently has—to sublicense such AT&T patents to competing manufacturers for use only in providing the BOCs with goods or services embodying the inventions of the patents, provided that such sublicense does not prejudice AT&T's existing cross license agreements.

grant sublicenses with respect to any other patents, for two reasons: first, because they may not, absent special permission, engage in new lines of business (sections II(D), VIII(C)), *e.g.*, the sale of patent rights simply as a business venture unrelated to their own use of the technology; and second, because AT&T's manufacturing competitors are not entitled, as such, to the fruits of the Bell System research (552 F. Supp. at 176-77).[120]

On the basis of these principles, it is convenient to consider the sublicensing issue with respect to two distinct categories of products or services—those which the Operating Companies will be allowed to market immediately upon divestiture, and those which they will not be permitted to market at that time.

The first of these categories includes, of course, customer premises equipment.[121] In an effort, accordingly, to resolve whether the grant of sublicenses to CPE patents by the Operating Companies to manufacturers of CPE would be used by the local companies in their provision of CPE—and whether therefore these companies

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[120] Several intervenors have suggested that the plan be modified to allow the Operating Companies to sublicense patents to manufacturers for the provision of goods and services not only to the Operating Companies but also to other purchasers, arguing that such broader sublicensing rights would result in increased royalty payments to the Operating Companies and, due to greater economies of scale, to the reduction in cost of all goods produced by independent manufacturers. See, *e.g.*, Reply of Wang Laboratories, April 13, 1983. The Court will not order such a modification, however, since it would, in effect, permit the Operating Companies to enter the patent licensing business.

[121] AT&T contends that the Operating Companies need not be granted rights to CPE patents in view of the Court's observation that the Operating Companies will enter the CPE market "from a zero base." AT&T Response to Objections at 465 n.* (citing 552 F. Supp. at 192 & n.248). There is nothing in the Court's language to support AT&T's conclusion; it merely justified the assignment to AT&T of the embedded CPE and the retail outlets.

may sublicense Bell System patents to such manufacturers—the Court has received and considered evidence (in both oral and affidavit form) from the chief executives of the Regional Companies. This evidence indicates that the Operating Companies will use the end products of the sublicenses in several respects.

First. The Operating Companies must have the right to sublicense CPE patents to manufacturers of their choice if they are to develop a CPE product line distinct from that of AT&T. As Thomas Bolger, designated chief executive officer of the Mid-Atlantic Region, has pointed out, if the Operating Companies were not granted rights to CPE patents, "the selection of the vendor to use Bell technology to supply a BOC would be taken from the BOCs and left to AT&T [which] might, or might not, cross-license the vendor with whom BOCs wish to deal."[122] Under such circumstances, the reliance of the Operating Companies upon Western Electric equipment would be perpetuated, thus impeding competition in the telecommunications equipment markets. It follows, of course, that without CPE patent rights and the ability to market a distinctive product line, the Operating Companies would not be able to provide the "effective counterbalance to AT&T's market strength" in CPE

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[122] Second Amended Certificate of Thomas Bolger, June 10, 1983, at 6. When questioned by the Court at the June 2, 1983 hearing as to whether the Operating Companies would use the CPE patents other than merely as a source of revenue, Bolger responded:

> I would use them in order to allow me the freedom to make arrangements with suppliers, if I wanted to and if I found that it would be valuable for me to do so, so that I would have additional flexibility to procure CPE for my requirements. . . . I'm not going to sell the technology. I want to use it to help me enter the CPE market.

Transcript at 25596.

marketing, which the Court sought to establish in modifying the decree. 552 F. Supp. at 192.[123]

Second. If the Operating Companies are able to sublicense CPE patents, they will probably be able to negotiate lower equipment purchase prices and thus to share in the benefits from the Bell System research which they supported for so long.[124] This, in turn, will facilitate greater CPE sales and higher Operating Company revenues, and contribute in the long run to the financial viability of the Operating Companies (and indirectly to stable local telephone rates).[125]

Third. The sublicensing of patents will permit the Operating Companies to benefit from increased competition among their suppliers—another development which would tend to reduce the price of CPE purchased by the

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[123] The logic underlying the licensing of all patents to the Operating Companies was to assure their independence from AT&T by providing alternative sources of supply for goods and services which they would use in the businesses which they were authorized to conduct. These companies had long been a captive market for Western Electric, both for telecommunications equipment and for CPE. Operating Company independence from AT&T is therefore crucial to CPE marketing, just as it is with respect to exchange and exchange access functions. With regard to both businesses the Operating Companies will be free to purchase equipment (or services) from suppliers which do not require licenses under AT&T patents; with regard to both businesses it is important, however, that they be able to purchase from alternative sources equipment (or services) which would not be available without sublicenses under AT&T patents.

[124] As indicated, the Operating Companies will be permitted to sublicense CPE patents only in order to enable a manufacturer to provide goods for resale by the Operating Companies. See *infra*. Thus, any royalty received by the Operating Companies under such sublicenses will, in all probability, be in the form of a reduced wholesale price paid by the Operating Companies to the manufacturer.

[125] See Statement of Wallace Bunn of May 23, 1983 at 5-7; Testimony of Thomas Bolger, June 2, 1983, transcript at 25596.

Operating Companies for resale. To the extent that greater competition among CPE manufacturers[126] and lower wholesale prices paid by the Operating Companies will result in lower retail prices for consumers, the public will benefit as well.

For these reasons, the Court concludes that the sublicensing of CPE patents to manufacturers of CPE would be a legitimate part of the Operating Companies' CPE marketing business.

In contrast to the substantive benefits which would inure to the Operating Companies from the ability to license CPE patents, only one possible adverse effect has been suggested.[127] The Department of Justice contends that Operating Company sublicensing of such patents would be a "step into the manufacturing area," contrary to section VIII(A) of the decree. Such sublicensing, according to the Department, would give the Operating Companies an interest in the success of their manufacturer-sublicensees, and this, coupled with the proprietary interest in the particular technology covered by the sublicense, would create an incentive for anticompetitive acts.[128]

In substance, this argument is but a variation of the claims made by the Department when it opposed the Court's decision to permit the Operating Companies to enter the CPE market. The Court then rejected the

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[126] There is no reason why an Operating Company would sublicense a particular CPE patent to only one manufacturer. See testimony of Thomas Bolger, June 2, 1983, transcript at 25597.

[127] To be sure, another consequence would be that AT&T would acquire additional competitors in the CPE business, but this could hardly be regarded as an "adverse" effect in the context of this antitrust decree designed, in part at least, to open the CPE market to competition.

[128] Department of Justice Response to Comments at 143-44.

Department's assertion[129] that Operating Company marketing of CPE would result in anticompetitive conduct,[130] because it concluded that the subsidization by the Operating Companies of their retail CPE operations with monopoly-derived revenues was entirely improbable.

There is no good reason—and the Department has offered none[131]—why the Operating Companies would have

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[129] At the same time, as the Court made clear, there are abundant reasons why the marketing of CPE by the Operating Companies is in the public interest (552 F. Supp. at 191-92).

[130] See 552 F. Supp. at 192; Memorandum of August 23, 1982.

[131] The Department has not attempted to explain how the grant to the Operating Companies of the right to sublicense CPE patents would increase the potential for cross-subsidization. The Department has, however, given three reasons why in its view discrimination among manufacturers could occur: (1) the sublicensing of patents would increase the Operating Companies' incentive to discriminate against certain vendors because the companies would have an incentive to market only the products of manufacturers operating under the sublicenses; (2) the Operating Companies would have the ability to extract concessions from manufacturers, thus undermining the potential for variety and merit purchasing; and (3) a financial interest in the success of a particular technology would enhance the incentives of the Operating Companies to develop standards through the CSO, which they own and control, to favor such technology. Department of Justice Memorandum, May 31, 1983, at 12-13.

The principal difficulty with these arguments is that there will be no reason for the Operating Companies to sublicense to only one particular manufacturer (and thus to favor that manufacturer's products) and a number of reasons why sublicenses will be granted to a number of manufacturers. See notes 126 *supra* and 134 *infra*. Additionally, the type of "concessions" the Operating Companies would extract from their sublicensing rights would be lower wholesale prices, which is hardly anticompetitive or contrary to the selection of vendors based on merit. Finally, if the Operating Companies were able to sublicense Bell System technology, more manufacturers would have access to this technology than if it were tightly controlled by AT&T, and it would be less likely rather than more so that the CSO would set standards that favored only AT&T and Western Electric products. See Independent Data Communications Manufacturers Assoc., Inc. Reply Memorandum, May 31, 1983, at 9 n.19.

a greater incentive or opportunity to engage in such subsidization merely because they will be able to sublicense CPE patents to independent manufacturers.[132] Such an ability would no more facilitate coordination between separate corporations likely to lead to cross-subsidization than the purchasing contracts themselves, nor would the sublicensing of patents make anti-competitive activities any less detectable.[133] See 552 F. Supp. at 191-92.[134]

Finally, it is surely not without significance that the manufacturers of CPE—whom the Department of Justice

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[132] Irrespective whether a sublicense is involved, the Operating Companies will share no common facilities with manufacturers. Further, sublicensing of CPE patents by the Operating Companies is no more a step into manufacturing than is the sublicensing of exchange and exchange access patents designed to provide goods and services to the Operating Companies for their exchange operations—yet the Department of Justice does not object to the latter. If Operating Company sublicensing of CPE patents were considered a form of manufacturing violative of the decree, then so presumably would the sublicensing of *any* patent by an Operating Company to a manufacturer—and the promises of AT&T and the Department of Justice made during the Tunney Act proceeding would be reduced to a nullity.

[133] See Memorandum of Midwest Regional Holding Co., May 23, 1983, at 20 n.20. It is difficult to see how sublicensing of patents would be a "step into manufacturing" likely to produce anticompetitive conduct also because the Operating Companies will, by necessity, have to negotiate with independent equipment manufacturers over a variety of contractual terms (*e.g.*, specification and design terms, volume contracts, trademark licenses) in order to obtain a distinctive line of products for resale.

[134] The Operating Companies will have no economic incentive to engage in discriminatory conduct merely because they will have the ability to sublicense. As they enter the CPE market with a zero market share, their overriding incentive will be to enter into arrangements with as many vendors as is necessary to produce the highest quality, lowest priced products for resale to the general public. And the Operating Company executives have given every indication to the Court that this is precisely what they intend to do.

is ostensibly attempting to protect—uniformly support the grant of sublicensing rights to the Operating Companies.

The Court concludes that the Operating Companies may sublicense their Bell System patent rights to manufacturers of CPE where the equipment produced under the sublicenses will be sold to the Operating Companies.

The same rule applies to the services which the Operating Companies will be authorized to perform. Clearly, they may sublicense patents for the manufacture of products which will assist them in providing intra-LATA service. Further, although prohibited from providing inter-LATA service generally, they will be in two relatively small areas of that market: corridor services[135] and Official Services.[136] Under the rationale applied to CPE, sublicenses may therefore be granted to manufacturers for the provision of equipment for the Operating Companies' own use in these two authorized inter-LATA services.[137]

Finally, section VIII(C) of the decree provides that the Court may, in the future, allow the Operating Companies to enter lines of business presently prohibited to them.[138] While, of course, the Operating Companies could not, immediately upon divestiture, sublicense patents useful

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[135] See pp. 294-95 *infra*.

[136] See pp. 273-81 *infra*.

[137] The Operating Companies will be responsible for ensuring that those to whom sublicenses are granted do not exceed the scope of the activities allowed hereunder.

[138] This may be done under that section, if it is demonstrated that "there is no substantial possibility that [an Operating Company] could use its monopoly power to impede competition in the market it seeks to enter."

with respect to such lines of business (see note 120 *supra*), the patent licenses assigned to them at the time of divestiture will become valuable through the automatic availability of the right to sublicense to the extent that section VIII(C) is successfully invoked in the future.[139]

C. General Considerations

Two additional considerations applicable both to the patent issue and the "Bell" name and logo questions deserve brief mention.

First. The Department of Justice[140] has been opposed to the marketing of CPE by the Operating Companies from the very outset. It was the Department which insisted on a provision in the proposed decree prohibiting such marketing. See, *e.g.*, Brief of the United States, June 14, 1982, at 30. When the Court on August 11, 1982, informed the parties that it would not approve the proposed decree unless that prohibition was eliminated, the Department sought reconsideration—the only issue with respect to which it made such an effort. See Memorandum, August 23, 1982. Finally, when the Court denied reconsideration, the Department, on the very date of filing the modified decree, submitted memorandum in

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[139] Until the occurrence of such an event, if ever, the particular patent licenses in the possession of the Operating Companies will simply lie dormant. AT&T will not be injured by the grant to the Operating Companies of licenses to patents which, ultimately, these companies may never utilize. There is also no need, therefore, to fear that the Operating Companies will use their patent rights to "peddle" AT&T technology. AT&T Memorandum May 23, 1982, at 23.

[140] Whether or not AT&T sought the Bell name and patent restrictions or was required or persuaded by the Department of Justice to agree to them, there can be no doubt that they are advantageous to AT&T, for they would, as a practical matter, eliminate competition from the Operating Companies or significantly curtail the effectiveness of such competition.

which it expressed "substantial doubts" that the modification allowing the Operating Companies to market CPE was "properly within the Court's authority under the public interest standard or [was] supported by the antitrust theory and the record in these cases."

The decree entered in this case allows the Operating Companies to market CPE. That decree was signed by the two parties, and it was entered as a judgment of this Court. Whatever may be the views of the Department of Justice or some of its officials regarding the wisdom of the CPE provision, it will be enforced. And the Court will not allow this provision to be stripped of its vitality by artificial restraints which would undermine the competitive position of the Operating Companies in the CPE business *vis-a-vis* AT&T.[141]

Second. The Court has previously taken note of the recent decision of the Federal Communications Commission concerning access charges. See 1983-1 Trade Cas. ¶65,333 at 66,973-75 (April 20, 1983). Briefly, the Court was advised prior to the entry of the decree that whatever subsidy from long distance rates might in the past have been inherent in the local rate structure could and would be preserved by means of access charges levied on interexchange carriers.[142] However, in December of last year, the FCC decided to levy such charges also on individual subscribers.[143]

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[141] *I.e.*, restraints which would unnecessarily and improperly deprive the local companies of the necessary and appropriate patent and trademark rights.

[142] That is, charges levied upon the carriers as a prerequisite to their obtaining access to the local loops and hence to the local subscribers.

[143] See *In the Matter of MTS and WATS Market Structure*, CC Docket No. 78-72 Phase I (adopted December 22, 1982). The FCC also decided to begin this program on January 1, 1984, the date of the reorganization of the Bell System. This effective date makes it appear that the imposition of this burden on consumers is related to the decree herein—which clearly it is not (see note 293 *infra*).

This access charge decision undermines one of the assumptions underlying the Court's approval of the decree[144]—that there would be no impairment of the principle of universal service[145]—that is, that everyone, regardless of income, would have access at least to a minimum of telephone service, in recognition of the fact that this service is a necessity rather than a luxury.[146] The FCC's decision unnecessarily[147] jeopardizes this objective.

Whatever its authority or lack of it with regard to this development,[148] the Court may certainly take into account, as further support for conclusions which are sound for other reasons. In passing upon the tradename, trademark, and patent issues, as well as on various other questions, the Court has done just that (see pp. 324-25 *infra*). In each instance, the Court's decision is fully justified by other, specific considerations cited in the text, but in each such instance the Court also found that

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[144] See 552 F. Supp. at 169, 224 n. 376.

[145] Universal service has been mandated by the Congress, and until December of last year it had been a principal policy goal of the Federal Communications Commission.

[146] One might consider, for example, such uses as the ability to reach fire, police, and other emergency services; the need of the elderly to reach physicians, close relatives, or others who might give them aid; and the desire of those in isolated areas of the country for contact with others.

[147] That decision, at bottom, rests upon the proposition that novel bypass technologies may erode the financial health of the Operating Companies, and that increased support from the residential ratepayers will allow these companies to remain competitive. There is no reason to believe that bypass on a large scale is imminent. Further, evolving technology may be expected to result overall in reduced costs. Rather than to serve as a basis for imposing a new burden on local ratepayers, such technology and such reduced costs would better be channelled to benefit all segments of the public, including the local subscribers.

[148] See pp. 326-27 *infra*.

its decision was buttressed by the need to cope with the threat posed to universal, low-cost, local telephone service.

## V

## EMPLOYEES

### A. Pension Plan

Two challenges are made to the employee pension provisions of the plan of reorganization.

#### 1. *Union Challenge*

The Communications Workers of America (Union)[149] claims that the plan's proposal to divide the Bell System Pension Plan (BSPP) into nine separate plans will materially alter the terms and conditions of employment within the Bell System, and that the plan therefore impermissibly interferes with the Union's right to bargain over pension benefits.

The two current pension plans, the BSPP covering nonmanagement employees and the Bell System Management Pension Plan (BSMPP) covering management employees, have existed in their present form only since 1980. Prior to that time, the many separate companies which constitute the Bell System administered separate pension plans. In October 1980 the plans were aggregated,[150] and even though a formal separation between management and nonmanagement personnel was maintained, the assets of both the BSPP and BSMPP have since 1980 been pooled for investment purposes into one Bell System Trust. The plan of reorganization would

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[149] Other labor unions are also involved, but they did not submit comments to the Court.

[150] The Union states that the decision to merge the various plans was a subject of collective bargaining, but AT&T disputes this assertion. AT&T Response to Objections at 399.

divide each integrated plan into nine plans to correspond to the nine entities which inherit AT&T's assets and functions after January 1, 1984.[151]

The Union, which is concerned specifically with the BSPP, offers eight changes it believes this division would cause, but upon examination they reduce to three general categories. First, the Union complains that the plan would phase out the "interchange" provisions in the BSPP governing the portability of service credit from one Bell System company to another. Second, it speculates that each of the nine plans will be financially more risky than the existing central plan,[152] with the result that an employee's benefits may be reduced. Third, the Union maintains that the post-divestiture plans—as described in the plan of reorganization—would treat former employees who are rehired differently from the way they now are treated for pension purposes.[153]

In approving the divestiture and rejecting the Union's request that the decree be modified to provide that it would not preclude continued national bargaining in telecommunications, the Court stated last August:

> [T]here is no need for such a modification. There is nothing in the proposed decree or in general prin-

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[151] For pension purposes, these nine entities are AT&T, the Central Staff Organization, and the seven Regional Companies.

[152] For example, the union posits that gains in one Operating Company's assets would no longer be available to compensate for losses in another Company's assets.

[153] A fourth criticism—that the distribution of the Trust's assets may be out of syncronization with the distribution of its liabilities, *i.e.*, the accrued benefits of employees—is plainly without merit. Elaborate actuarial studies will be performed after employee assignments have been finalized to ensure that pension assets in the appropriate amounts follow each employee. A company would therefore not receive a disproportionate number of employees near retirement without also receiving a proportionately greater amount of pension assets.

> ciples of law which would preclude or interfere with such bargaining, and there accordingly is no reason whatever why, following the entry of the decree and the reorganization, such bargaining cannot continue as in the past.
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> [T]he settlement of the lawsuits . . . do[es] not involve AT&T's labor relations and, more particularly, [it has] nothing to do with the Communications Workers of America or its relationship with the Bell System. [citations omitted]. It follows that the union, on the one hand, and AT&T, and the divested Operating Companies, on the other, will be entirely free to arrange their mutual labor relationships as the Bell System and the union did in the past, irrespective of the structural changes that may be brought about by the decree.

552 F. Supp. at 210.

The Union cites this language, the labor exception to the Sherman Act, federal labor policy, and the lack of relation between the Bell System Pension Plan and AT&T's alleged anticompetitive conduct as reasons why the Court should not approve the plan's proposed treatment of the BSPP but should commit the future of the BSPP to the results of collective bargaining.

First. The Court observes that the plan of reorganization does acknowledge the role of collective bargaining over pension benefits. AT&T states that

> [t]he provisions of this section [regarding pensions] are based on the Bell System's plans and trusts as they currently exist. These plans and trusts may be modified during 1983 or thereafter as a result of collective bargaining or other requirements.[154]

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[154] Plan of Reorganization at 281 n.317. Moreover, AT&T and the Union have already bargained over certain effects of divestiture on employees' pension and health benefits, and the results of this bargaining are reflected in the Amended New Entities Arguments dated March 26, 1982, March 30, 1982, and April 5, 1982. See AT&T Response to Objections at 397.

Thus, it does not appear that AT&T is attempting to ride roughshod over the bargaining rights of its employees.

Second. Although AT&T could not materially alter pension benefits unilaterally (see *NLRB* v. *Katz*, 369 U.S. 736 (1962), *Bastian-Blessing, Division of Golconda Corp.* v. *NLRB*, 474 F.2d 49 (6th Cir. 1973)), this principle and the cases which support it are inapplicable here.[155] We are not dealing here with unilateral employer action in the sense in which it is condemned by the labor laws, but with a break-up of the employer company as part of a comprehensive settlement of a complex antitrust action. See *Newspaper Guild of Greater Philadelphia, Local 10* v. *NLRB*, 636 F.2d 530, 560 (D.C. Cir. 1980).

Furthermore, contrary to the Union's assumption, the decree in this case requires far more than a separation of AT&T's telecommunications functions; it requires the complete economic separation of the various components of the Bell System. See, *e.g.*, sections I(A)(1); I(A)(3). It would be entirely inconsistent with the decree to perpetuate a unified pension plan, with the result that employees of the independently owned and functioning Operating Companies would continue to look to AT&T for their pension benefits. As it is, equipment manufacturers are concerned that they may not receive equitable treatment from Central Staff Organization employees due to their alleged emotional ties to their former parent company. Such claims would acquire considerable plausibility if CSO and Operating Company employees

[155] In *Katz*, the Supreme Court held unlawful an employer's unilateral establishment of new systems of wage increases, sick leave provisions, and merit raises at a time when it was negotiating with the union regarding the same subjects. *Bastian-Blessing* likewise involved the unilateral termination by the employer of a health insurance plan which had been the subject of collective bargaining. Neither case even remotely resembles the facts of the instant situation.

believed that they had a continued economic stake in AT&T in the form of their retirement benefits.

At a minimum, the decree requires that the pension assets of employees follow them to their new assignments, and that the Regional Companies develop, as soon as possible, self-sufficient pension plans.[156] Union-employer bargaining for a continued, unified pension plan is thus not a viable option. This is a structural matter covered by the decree that is not inconsistent with federal labor policy, for there will be no "changes in coverage, levels, or administration of the plan." *Connecticut Light & Power Co.* v. *NLRB*, 476 F.2d 1079, 1082 (2d Cir. 1973).[157]

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[156] AT&T proposes to continue to administer the pension plan of any Regional Company that requests such "full service" assistance for a transition period during which the Company would acquire the skills and resources to manage its own pension plan. Regional Companies that request this option would receive their share of pension assets no later than 1987. Plan of Reorganization at 297. The Court approves of AT&T's continued management of a Regional Company's pension plan with the expectations that the Regional Companies choosing this option will have as much authority over their respective plans while they are technically under AT&T's administration as they desire, and that the transition periods will be kept to a minimum. It would be impractical to insist that assets be immediately transferred to a company that does not believe it can prudently manage them. At the same time, continued linkage between AT&T and the Regional Companies is not to be encouraged. In this regard, AT&T proposes to continue managing the Bell System Trust's real estate investments, which amount to approximately $3.1 billion. The Court approves this aspect of the plan, although reluctantly, in view of the nonliquid nature of these assets and the allowance for a Regional Company or AT&T to buy out of the arrangement.

[157] AT&T and the Department of Justice represent that this will be the case: benefit amounts and entitlement and eligibility requirements will not change. The financial performance of the individual plans may vary but the Union has offered nothing but speculation that any such variation would have an actual effect on the level of benefits, particularly since the fair market value of the BSPP and BSMPP trusts exceeds the present value of accrued benefits. Plan of Reorganization at 295 n.332.

The phasing out of unlimited portability[158] is likewise a natural consequence of divestiture, for it would surely be inconsistent with the independence of the Operating Companies from AT&T and from one another to allow employees to rotate among them as freely as if these companies were related entities.[159] The Court therefore approves AT&T's proposals which would divide the two existing plans into nine separate plans, and the provisions governing the division of pension assets through actuarial studies—both before and after divestiture—to ensure that the assets will be equitably distributed.

Third. There is merit in the Union's position that the Court need not and should not involve itself in the specific terms of the post-divestiture pension plans beyond their structure. Unlike the threshold issues of the pension plans' division and the elimination of unlimited portability, the precise terms of the pension plans admit

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[158] Under the plan, unlimited portability would remain in effect for one year after divestiture, except that employees in certain specified job categories who work on facilities shared by the Operating Companies and AT&T would be granted longer portability entitlements. See *infra* at 271. Portability would continue after the one-year "true-up" period among the Operating Companies controlled by each Regional Company.

The Union objects to the elimination of unlimited portability insofar as it overrides a benefit secured previously through collective bargaining. AT&T agrees with the Union that "many of the employee protections to be provided during the true-up period are subject to collective bargaining" (AT&T Response to Objections at 382 n.*) but argues that the decree requires the parties and the Court to set a definite time limit for the true-up period. The Court agrees that the decree's separation between AT&T and the Operating Companies requires the establishment of a fixed true-up period for employee transfers, and it finds that the one year proposed in the plan is reasonable. To the extent that it might be thought that this provision affects collective bargaining rights, such rights are superseded by the Court's power to enforce its decree. *Cf. Franks* v. *Bowman Transportation Co.*, 424 U.S. 747 (1976).

[159] See, *e.g.*, Comments of Satellite Business Systems, filed Feb. 15, 1983, at 65.

of several resolutions each of which would be consistent with the decree.[160] However such nonstructural aspects of the pension plans may have been resolved in the past, their resolution is not cast in concrete. Accordingly, they are open for further decision, whether by collective bargaining when the contract governing the current pension plan expires in August 1983, or otherwise as AT&T and the Union see fit. The Court's approval of the plan of reorganization is therefore not to be regarded as an endorsement of whatever AT&T may be planning with respect to post-divestiture pension benefits. To put it another way, there is nothing in the Court's approval of the plan of reorganization (other than the structural and portability matters discussed above) which would in any way impair the obligation of AT&T to bargain in good faith with the Union.

2. *State Objections*

The State of Maine and the Maine Public Utilities Commission argue that the plan of reorganization improperly allocates certain pension assets to AT&T. Under the plan, the assets of BSPP and BSMPP would be divided and allocated among the nine post-divestiture entities so that the accrual rates[161] for each of the new plans after divestiture would be approximately the same as will be the rates under the AT&T plans immediately prior to divestiture.

The allocation would be accomplished in two steps: first, there would be coverage of an amount equal to the

[160] There is nothing in the provisions of the decree governing, for example, the treatment by the post-divestiture plans of former employees who are rehired, or what rules ought to determine when an employee's pension rights become vested.

[161] An accrual rate is the percentage of total payroll that must be contributed to a plan periodically in order to meet future pension liabilities.

present value of accrued benefits for each participant; second, all remaining assets—the difference between the present value of assets and liabilities—would be allocated so that the accrual rates for the post-divestiture pension plans would be approximately the same as the accrual rates in effect for the AT&T plans immediately prior to divestiture. Maine does not quarrel with the first step which, in any event, is required by the Employee Retirement Income Security Act (ERISA) and section 3414(1) of the Internal Revenue Code. However, in its view, the assets in excess of those needed to cover accrued benefits[162] should be allocated in proportion to the contributions which produced the excess rather than on the basis proposed by AT&T.

Maine claims that because some 10 to 20 percent of present Operating Company employees will be transferred to AT&T,[163] it is likely that excess assets originally contributed to the pension plans by the Operating Companies will improperly be transferred to the AT&T plan (thus reducing proportionately its pension liabilities).[164]

It may well be true, as Maine contends[165] that the law does not affirmatively require that excess assets must

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[162] According to AT&T's 1982 Annual Report (p. 38), the fair market value of the pension assets exceeded the present value of accrued benefits by more than $11.5 billion.

[163] This is due to the separation of interexchange and CPE operations from the Operating Companies. Plan of Reorganization at 456 n.430.

[164] To the extent that some entities (either AT&T or an Operating Company) had proportionately more excess than others, the plan would equalize the extent of any such excess regardless of which Operating Company was the source of the overfunding.

[165] Reply of Maine and Maine PUC, April 13, 1983, at 19.

follow the transferred employees from the Operating Companies to AT&T since there is no requirement that employees receive the benefit of excess assets.[166] What is flawed, however, is the State's argument that it is improper for the plan of reorganization to allocate the excess funds in accordance with future payment obligations and contribution levels, and that these funds must be allocated instead in accordance with the contributions made in the past. What this argument overlooks is that while the Operating Companies would be losing excess assets associated with the transferred employees, they would also be losing liabilities, *i.e.*, the benefits the employee will accrue in the future. Under Maine's proposal, entities with higher liabilities after divestiture than before would have fewer pension fund assets to meet their future obligations, requiring a higher funding rate. Conversely, those companies which will have lower pension liabilities after divestiture than before would enjoy a windfall. The most important consideration is the interest of the participants and beneficiaries,[167] and they are best served by the proposed plan.[168]

B. Employee Transfers

In addition to the one-year true-up period[169] immediately following divestiture during which any employee may be transferred between AT&T and an Operating Com-

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[166] See, *e.g.*, *Washington-Baltimore Newspaper Guild Local 35* v. *Washington Star Co.*, 555 F. Supp. 257 (D.D.C. 1982); Rev. Rul. 83-52, 1983-13 I.R.B. 7; see also ERISA §4044(d)(1).

[167] See ERISA, §404(a)(1); *Donovan* v. *Bierwirth*, 680 F.2d 263 (2d Cir. 1982).

[168] There is also no evidence to support the assumption that the Operating Companies will have contributed to excess funds in greater proportion than has AT&T.

[169] See note 158 *supra*.

pany[170] without loss of seniority rights or other benefits,[171] the plan further provides that employees in four specific job categories[172] may be transferred without loss of benefits after the one-year period.[173]

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[170] It may be noted that all the transfers during the true-up period will be the result of arm's length negotiations between AT&T and the Operating Companies, and there is thus no occasion for either a "post-divestiture re-evaluation plan," judicial involvement, or the appointment of special Operating Company representation, as some have suggested. *E.g.*, Comments of the State of Michigan and Michigan Public Service Commission, Feb. 11, 1983, at 30; Comments on AT&T's Plan of Reorganization of the Public Service Commission of the State of Missouri, February 15, 1983, at 14. It is unclear what representation could be provided by the Court for companies which, after divestiture, will be independent entities. If the true-up process is not being conducted in accordance with the decree and the plan, ample means will be available for corrective action.

[171] The Court expects, as AT&T represents, that the one-year true-up period will not be used for frequent personnel transfers but as a "time for correcting mistakes that are bound to occur in a reorganization of this magnitude." AT&T Response to Objections at 378.

[172] These categories are (1) Operating Company service center employees who will write inter-LATA orders for AT&T under a sharing contract until such time as the contract ends and they are reassigned to AT&T, but no later than 5½ years after divestiture; (2) AT&T operators who will provide intra-LATA Call Completion and Assistance services until Operating Companies establish such systems and they are reassigned to the Operating Companies, but no later than 10½ years after divestiture; (3) Operating Company personnel who will provide circuit provisioning functions for AT&T until AT&T assumes this responsibility, but no later than 5½ years after divestiture; and (4) employees providing installation and maintenance services for "special services" both by AT&T for Operating Companies and vice versa, until the companies provide their own services, but no later than 5½ years after divestiture. AT&T claims that, for various reasons, it would be inefficient for AT&T and the Operating Companies to provide these functions independently immediately upon divestiture. See AT&T Response to Objections at 388 n.*.

[173] Under the plan, the duration of the transfer is limited to the period necessary to accomplish the change of multifunction facilities to exclusively AT&T or Operating Company facilities. This will occur not later than five years and six months after divestiture, except for operator services personnel who may be transferred up to ten years and six months after divestiture. Plan of Reorganization at 287-88. See note 172 *supra*.

Section I(A)(2) of the decree provides that AT&T and the Operating Companies may continue to share certain facilities, and the plan implements that provision by specifying that the entities "intend to cease sharing network facilities as promptly as is reasonably feasible." Plan of Reorganization at 56. The plan's employee transfer provisions are justified by AT&T on the basis that the job functions of these employees will begin with one entity but will need to be transferred to another as transitory arrangements for the sharing of multifunction facilities are phased out. Response to Objections at 382-83.

The principal objections raised to the plan's grant of transfer rights to the employees are that this may result in fraternization between AT&T and Operating Company personnel, the disclosure of equal access network information to AT&T employees, the perpetuation of loyalty to the Bell System, and the provision by Operating Company personnel of certain interexchange services to AT&T but not to other interexchange carriers. See, *e.g.*, Comments of Satellite Business Systems, February 15, 1983, at 65-66, 91.

The intervenors' concerns are not frivolous; however, given the necessity for some sharing of multifunction facilities, the solution adopted in the plan is, in general, a reasonable one. The basic alternative to the provisions for transfers without loss of benefits is a lay-off of the affected employees by one entity to be followed by a (possible) rehire by the other. The Court has no intention whatever of unnecessarily imposing such a hardship on these employees. Moreover, the entire matter must be kept in perspective: the individuals involved will not be managers or other policy makers but relatively low level employees. It is thus unlikely that manipulation or the disclosure of sensitive information to AT&T will occur.

The loss of employment security and the unusual and unnecessary inefficiencies which would be the consequence of a rejection of most of the transfer provisions can therefore not be justified.

There is, however, one exception to this principle. AT&T has not demonstrated why Operating Company personnel should write inter-LATA orders for AT&T for up to 5½ years after divestiture. Such order-writing is purely an interexchange function; it is performed by persons, not "facilities" as that word is used in section I(A)(2); and this service would not be available to any interexchange carrier other than AT&T. Indeed, such order-writing by Operating Company personnel for AT&T could provide the latter with a significant competitive advantage. The Court will not permit sharing of this function, and it will require the deletion of references to such sharing from the plan of reorganization (at pp. 253, 254, 279-80, and 287), unless the benefits are made available to all interexchange carriers.

The Union, unlike the other intervenors,[174] suggests that the Court require modification of the plan to permit unlimited transfers of employees among the post-divestiture Bell System entities. As noted *supra*, such a provision would be flatly inconsistent with section I(A) of the decree and with the underlying rationale of the judgment—that the economic integration among the various Bell System entities must cease. That proposal, too, will therefore be rejected.

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[174] However, the State of New York would permit all employees in shared services to have and exercise transfer rights, as distinguished merely from the four categories of employees listed in the plan.

## VI

## Official Services and Other Facilities

With one major exception, the division of network facilities and other assets is reasonable and fully consistent with the decree.

### A. Official Services

The Court will not approve the decision made in the plan of reorganization with regard to so-called Official Services. These services represent communications between personnel or equipment of an Operating Company located in various areas and communications between Operating Companies and their customers.[178] The plan of reorganization provides that Bell System facilities used in whole or in part for Official Services will be assigned according to the same rules applicable to other transmission facilities; meaning that, if facilities

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[178] There is some dispute as to whether Official Services are limited to Operating Company internal communications or whether they include communications between an Operating Company and its customers. See AT&T Response to Objections at 95-96 n.*; Supplemental Affidavit of William Weiss, April 12, 1983, at 9; letter from Raymond Burke, April 13, 1983, at 2 n.*.

The Court concludes that for purposes of the discussion and decision herein "Official Services" must properly include customer communications. As Raymond Burke points out (April 13, 1983 letter at 3 n.*),

> no charges apply to communications which AT&T classifies as 'official' service . . . [and] even where there is a charge for such services as directory assistance, any inter-LATA administrative facilities involved are not 'for hire.'

Similarly, Thomas Bolger notes (Amended Certification of April 6, 1983, at 5-6),

> a customer in Salisbury, Maryland actually speaks to a directory assistance operator in Baltimore, but that is done solely to facilitate the conduct of these exchange operations in efficient work groups. The customer does not care where his call is answered and he pays no charge for the referral of his call from a local central office to a distant company location for this purpose.

are used solely or predominantly to perform inter-LATA functions, they will be assigned to AT&T even if the functions constitute Official Services.[176] Additionally, the Department of Justice has indicated to one or more Operating Companies[177] that it would object if they constructed and operated their own inter-LATA facilities to administer Official Services.[178] In the view of the Court, neither the plan's treatment of Official Service facilities nor the position of the Department of Justice is consistent with the principles underlying the decree.

Each Operating Company conducts its authorized operations in several LATAs. In order to achieve operational efficiencies, the four basic categories of Official Service systems[179] have been designed to serve

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[176] See AT&T Response to Objections at 95-96.

[177] The several communications from the Department of Justice to the Operating Companies may not be entirely consistent with regard to this subject, however.

[178] See Amended Certification of Thomas Bolger, April 6, 1983, at 5; letter from Raymond Burke, April 13, 1983, at 1.

[179] The Operating Companies manage their business through the following complex networks for the transmission of voice and data communications:

(1) The Operational Support System Network is a network of dedicated voice and data private lines used by the Operating Company to monitor and control trunks and switches. These communications links are vital to the proper operation of the network since, for example, they enable Operating Company personnel to measure the maintenance status of trunks and switches and instantly to control equipment and reroute traffic.

(2) The Information Processing Network is a network of dedicated data lines linking the Operating Companies' information system computer. It is used to transmit data relating to customer trouble reports, service orders, trunk orders from interexchange carriers, and other information necessary for carrying out the Operating Companies' business.

(3) Service Circuits comprise a network of largely dedicated voice lines used to receive repair calls and directory assistance calls from Operating Company customers. These communica-

geographical areas which are usually larger than individual LATAs. For example, the so-called "Operational Support System Networks" (see note 179 *supra*) typically cover an entire state or major portion of a state, permitting the monitoring and controlling of trunks and switches and the routing of traffic from a centralized location. Directory assistance, repair service offices, and business offices likewise serve geographical areas which are larger than individual LATAs.[180]

For the reasons stated below, it makes no sense to prohibit the Operating Companies from using, constructing, and operating on their own the facilities they need to conduct Official Services, whether they be intra-LATA or

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tions ensure the maintenance of telephone service and they provide directory assistance to Operating Company customers.

(4) Voice communications are used by the Operating Companies for hundreds of thousands of calls relating to their internal business.

Supplemental Affidavit of William Weiss, April 12, 1983, at 11-12.

[180] As Thomas Bolger, designated chief executive of the Mid-Atlantic Regional Company, has pointed out:

> In order to reduce costs and maximize efficiency, the BOCs have computer processing centers which receive billing and other data from company locations in a number of LATAs. Similarly, calls from Operating Company customers seeking such services as directory assistance are currently routed between BOC offices to centralized locations in other LATAs.

Amended Certification of Thomas Bolger, April 6, 1983, at 5.

inter-LATA in character, and to require them instead to lease such facilities from AT&T.[181]

The Department of Justice recognizes "that the BOCs may have constructed their internal data processing and operational support systems on the assumption that communications links between their facilities would be over BOC-owned facilities,"[182] and further that to require such communications to be "placed on commercial facilities might abruptly increase the BOCs' cost of providing service."[183] Yet, relying solely on the curt rationale that such traffic is correctly classified as inter-LATA, the Department supports the assignment of all existing inter-LATA Official Service facilities to AT&T. This solution is both unwise and unnecessary.

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[181] The Department of Justice suggests that where Operating Company facilities are transferred to AT&T under the assignment process, it would be appropriate for AT&T to lease back to the Operating Company those circuits currently dedicated to Official use. However, an Operating Company's ability to lease existing Official Service facilities from AT&T would be limited to the duration specified in the plan of reorganization for shared facilities—that is, eight years. See Department of Justice Response to Comments at 35; AT&T Response to Comments at 115; Amended Certification of Thomas Bolger, April 6, 1983, at 5. After this eight-year period, the Operating Companies would have to hire the services of AT&T or other interexchange carriers to meet all their inter-LATA Official Service needs.

[182] Department of Justice Response to Comments at 35. Indeed, ironically, in spite of the fact that most Operating Company Official Service communications are presently conducted over facilities "owned" by these companies themselves, many such facilities would now, under the plan, be assigned to AT&T. Supplemental Affidavit of William Weiss, April 12, 1983, at 10.

[183] Department of Justice Response to Comments at 35. However, that is precisely what will happen in eight years under the Department's scheme. See note 181 *supra*. Even during this eight-year period, any Official Service demands which cannot be satisfied by existing circuits leased from AT&T would have to be "placed on" commercial facilities of an interexchange carrier.

Only two alternatives would be available to the Operating Companies under the current plan, both of them undesirable. One option would be for the companies to redesign their Official Service systems so that none of their internal communications crosses LATA boundaries. This would result in a loss of the operational and cost efficiencies produced by the centralization which currently exists in the local phone system.[184] In effect, a separate, self-contained Operating Company would be created for each LATA—a result clearly not contemplated by the decree.

The other option would be to have the Operating Companies' Official Service communications carried by AT&T or another interexchange carrier. See note 181 *supra*. This alternative would not only be very costly[185] but it suffers from a number of other infirmities. As William Weiss, chief executive-designate of the Midwest Region, points out:

> Speed and reliability are critically important with respect to the BOCs' monitoring and controlling of their switches and trunks. BOC operating personnel and computers must have continuous, instantaneous information regarding traffic loads and the operating status of equipment. When traffic overloads or equipment malfunctions occur, they must have the capability to immediately control equipment and reroute traffic. Forcing the BOCs to rely on third parties for official service communica-

[184] In recent years, many of the Operating Companies have achieved significant cost savings through the modernization of their internal management processes. Supplement to Sworn Statement of Wallace Bunn, April 7, 1983, at 5 (47,000 internal computer terminals in operation throughout Southeast region alone).

[185] It has been estimated that for the Mid-Atlantic region alone, the total expenditures for all types of inter-LATA Official Services would be approximately $125 million annually. Amended Certification of Thomas Bolger, April 6, 1983, at 6.

> tions . . . could seriously jeopardize the BOCs' fulfillment of their responsibilities to provide intra-LATA communications and exchange access. . . .
>
> Moreover . . . [i]n many instances, the BOCs could more efficiently conduct these communications over inter-LATA facilities constructed and owned by the BOCs. The BOCs' ability to deploy new transmission technologies is at least as good and probably better than that of third parties who might provide us with inter-LATA services. The cost of building facilities utilizing those new technologies might be far less than the cost of leasing facilities employing older, and thus higher-priced technologies.
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> . . . The critical point is that the BOCs should be free to conduct their official services communications in the optimal manner, selecting whichever option is the most reliable and cost-efficient.[186]

Such significant burdens should not be imposed on the Operating Companies unless this is clearly required by the decree. An examination of the decree's provisions shows, however, that a prohibition on the maintenance of inter-LATA Official Service facilities by the Operating Companies is required neither by its spirit nor by its letter.

The Operating Companies are prohibited from engaging in intercity, inter-LATA services in order to prevent a recurrence of the alleged anticompetitive practices of AT&T, which was claimed by the government to have used its local monopolies to disadvantage its intercity competitors in a variety of ways. That rationale is wholly inapplicable to the provision of inter-LATA service by

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[186] Supplemental Affidavit of William Weiss, April 12, 1983, at 13-14. An increasing number of private corporations with operations dispersed over large geographic areas, such as oil companies and electric power utilities, have opted to construct and operate their own circuits by which their administrative communications are transmitted. Letter from Raymond Burke, April 13, 1983, at 2; see also, Amended Certification of Thomas Bolger, April 6, 1983, at 6; Supplement to Sworn Statement of Wallace Bunn, April 7, 1983, at 6.

each Operating Company for its own internal, official purposes.[187] Only by a highly abstract distinction between services that are once and for all labelled "competitive" or "monopolistic" could that prohibition be applied to the Operating Companies' Official Services. Moreover, it is ironic that a prohibition which grew out of AT&T's dominant competitive position and its alleged misuse of that position is now sought to be applied in such a way as to afford AT&T a substantial financial benefit by giving it the opportunity to carry, for a profit, the Operating Companies' own internal, official communications which these companies are perfectly able to carry themselves and have, indeed, carried themselves in the past.[188]

Nor is so illogical a result required by the strict terms of the decree. While the Operating Companies are prohibited by section II(D)(1) from providing "interexchange

[187] The Operating Companies are prohibited from providing inter-LATA telecommunications services under the decree for two reasons: the possibility of discriminatory interconnection practices and the possibility of subsidization of interexchange services with revenues from local exchange services. See 552 F. Supp. at 188-89. Neither of these reasons is implicated by the ownership and operation by an Operating Company of its own inter-LATA Official Service network.

[188] There is also a distinct possibility that AT&T might be able to gain competitive advantages from its control over Operating Company official circuits. Compare 552 F. Supp. at 181 (possible advantage to AT&T from control of electronic publishing business).

In arguing that the Operating Companies should be able to construct and operate their own inter-LATA Official Service facilities, Raymond Burke wrote on April 13, 1983, at 4:

> Indeed, to the extent that the BOCs would need to purchase materials from facilities vendors in order to construct microwave, fibre, and other facilities for their administrative use, it would appear that competition in such markets would be enhanced. In contrast, the Department's interpretation may create a situation in which the BOCs may, practically speaking, be able to obtain their administrative facilities from only one interexchange carrier—AT&T.

telecommunications services," section IV(P) defines "telecommunications services" as "offering *for hire* of telecommunications facilities" (emphasis added). Obviously, the Official Services are not "for hire." Similarly, the decree prohibits the Operating Companies from engaging in "information services," but it expressly permits them to engage in such services "for the management, control, or operation of a telecommunications system or the management of telecommunications service." Section IV(J). Further, section I(A)(1) mandates

> [t]he transfer from AT&T and its affiliates to the BOCs . . . of sufficient facilities [to permit them] to perform, independently of AT&T, exchange telecommunications and exchange access functions, including the procurement for, and engineering, marketing and *management* of, those functions. (emphasis added).[189]

In light of these provisions, it is thus not surprising that, contrary to its present position, the Department of Justice stated in its competitive impact statement filed with the Court on February 10, 1982, that the Operating Companies will continue to perform those functions which are "inherent" in exchange communications and exchange access, such as "the ability to engage in the . . . management of retained functions." Competitive Impact Statement at 29. Because each Operating Company will perform its authorized services in several LATAs, an

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[189] AT&T argues to the contrary that section VIII(G) calls for the assignment to it of facilities which perform both intra-LATA and inter-LATA functions if the use for inter-LATA functions predominates. AT&T Response to Objections at 97. However, that section does not speak at all of inter-LATA and intra-LATA functions but states more simply that

> facilities . . . which serve both AT&T and one or more BOCs shall be transferred to the separated BOCs if the *use* made by such BOC or BOCs predominates over that of AT&T (emphasis added).

inherent part of the management of those services includes official communications which cross LATA boundaries.

For those reasons, the Court rules that an Operating Company shall receive inter-LATA facilities which are used solely or predominantly for the performance of its own Official Service functions. If the use made by an Operating Company of a multifunction facility for the provision of exchange telecommunications, exchange access, and Official Services, predominates in the aggregate (including all such functions) over that made of such facility by AT&T, the multifunction facility is required under section VIII(G) of the decree to be assigned to the Operating Company.[190] The Court further confirms that the decree does not prohibit the Operating Companies from providing their own Official Services, including, if necessary, by the construction of the appropriate inter-LATA facilities.[191]

B. Other

The network assets are being assigned on the basis of whether they provide an exchange function (in which event they are assigned to the Operating Company) or an interexchange function (in which event they go to AT&T); where an asset performs both functions, the assignment depends essentially upon predominant use. Sections I(A)(2), VIII(G); see note 20 *supra*.

A number of intervenors have objected to one aspect or another of the division of assets provided for under

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[190] It may be that this provision will not have a significant effect on the assignment of assets because Official Services use may not often tip the scales as between inter-LATA and intra-LATA use. See AT&T Response to Objections at 99.

[191] The Court reaches this question now, rather than after divestiture, so that the Operating Companies may be able to continue their essential network and operational planning.

the plan (or to the failure to complete such division in advance of the approval of the plan of reorganization) but the Court finds all such objections (other than those related to Official Services allocations discussed *supra*) to lack merit.

1. Several intervenors claim that the plan improperly disregards the predominant use test required by the decree. To be sure, the decisive role of that test can most clearly be discerned in the assignment of switching systems, and its role is not as apparent where less complex equipment is involved. That result, however, is not surprising: it would be technically and administratively impossible to assign ownership of each of the thousands of relatively small items in the central offices on the basis of predominant use. What AT&T has proposed instead is to assign equipment bays containing related items of equipment to work areas which, in turn, are assigned to AT&T or the Operating Companies on the basis of predominant use. In the absence of a showing that the assignment of the general work areas as such is not being made on this basis—which has not been forthcoming—the Court will accept these provisions of the AT&T plan.[192]

2. The assignment of the private line facilities and other specialized functions (*e.g.*, call completion and local directory assistance) proposed in the plan is likewise con-

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[192] The Court likewise finds not unreasonable AT&T's decision to consider predominant use as of January 1, 1984, rather than as of some earlier date, as several intervenors have suggested. Network changes are, of necessity, occurring all the time, and most of them appear to have been planned, and partially implemented, for some time, in some instances for years. The suggestion that the January 1, 1984 date gives AT&T an undue opportunity for manipulation is unrealistic and unwarranted.

sistent with the decree and otherwise appropriate, and it will therefore also be approved.[193]

3. One type of facility about which there has been particular controversy is 800 Service Directory Assistance which several of AT&T's competitors claim properly to belong to the Operating Companies. It is abundantly clear, however, that this particular directory assistance is an interexchange, inter-LATA service which is appropriately assigned to AT&T. If this enhanced service were assigned to the Operating Companies in spite of the fact that it performs interexchange functions, it could be done only on the basis that AT&T's competitors should be afforded the ability, through the medium of the Operating Companies, to offer this service without having to pay for it.[194] If the other interexchange carriers wish to offer long distance directory assistance, they will have to construct the necessary facilities. It is not the purpose of the Court's review of the plan to reorganization to "punish" AT&T or to provide advantages to its

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[193] Several intervenors had originally objected to the plan's assignment of Digital Dataphone Service (DDS) facilities to AT&T. Subsequently AT&T accepted the Department of Justice's position with respect to such facilities, and it now appears that all DDS hubs, which were the focus of the intervenor's objections, will be assigned to the Operating Companies. See Department of Justice Supplemental Response, June 1, 1983, at 7. Additionally, the Department has made a commitment to review the contracts for the sharing of DDS facilities to ensure that the Operating Companies will have the ability to afford equal access to these facilities to all interexchange carriers. *Id.* at 8 n.*. The Court, therefore, finds the assignment of DDS facilities to be consistent with the decree.

[194] Unlike with respect to some other subjects (*e.g.*, the Cambridge switch discussed at pp. 204-05 *supra*) there is no reasonable basis for departing from the predominant use rule.

interexchange competitors to which they are not legitimately entitled.[195]

The assignment of the network facilities and other assets provided for in the plan of reorganization will accordingly be approved.

## VII
## LATA Issues

In its April 20, 1983 Opinion on the proposed LATAs (see note 6 *supra*) the Court requested further information with regard to certain specified LATAs as well as assurances with regard to intra-LATA equal access. Also to be resolved at this time are issues which have been separately briefed respecting traffic between the LATAs and areas served by non-Bell, or independent telephone companies.

### A. Individual LATAs

#### 1. *Vermont, Maine, New Hampshire*

The Court in its April 20, 1983, Opinion declined to approve New England Telephone's proposed departure of

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[195] It should also be noted that the plan of reorganization initially assigned "Charge-A-Call" public telephones to AT&T on the ground that they are used predominately for inter-LATA communications. However, a number of intervenors, along with several designated chief executives of the Regional Companies, objected to this assignment, arguing that despite the inter-LATA nature of the calls placed over these telephones, they are exchange facilities, having been installed by the Operating Companies as part of the service they provide to the public. The Department of Justice concurred with these objections, and required the plan to be modified to assign Charge-A-Call public telephones to the Operating Companies. See Department of Justice Response to Comments at 82-83. This modification was agreed to by AT&T and has been incorporated into the plan of reorganization. The Court concurs with this modification. Pursuant to the plan as so modified, the Operating Companies will be able to provide users with access to several interexchange carriers, while under the original plan AT&T would have limited access through these public telephones to its own long distance network.

the Maine, Vermont, and New Hampshire LATAs from state boundaries because some 26 border communities would otherwise have been placed in "out-of-state" LATAs.[196] The regulators in these states had expressed concern that these stateline crossings could result in discriminatory treatment of telephone users in these communities, and they requested that these areas be redrawn so that each LATA would correspond precisely to the borders of the particular state. NET has since informed the Court that it withdraws its request for stateline crossings and proposes instead LATA boundaries which conform to state borders. These new LATAs are approved.[197]

NET requests additionally that it be allowed to phase in the new LATA boundaries, so that, in order to minimize costs, the necessary network modifications may be undertaken in conjunction with other system improvements.[198] That request is likewise approved.[199]

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[196] These communities are presently served by NET facilities located outside the particular state, and NET requested the stateline crossings in order to continue these serving arrangements.

[197] The network reconfiguration costs and other network considerations are not so significant as to outweigh the discriminatory treatment of and the inconvenience to residents in these communities.

[198] The regulatory commissions support this request. Additionally, Vermont wishes the Court to declare that these costs ought to be recovered through carrier access charges rather than through local rates. This is, of course, a matter for the regulatory commissions to execute, but the Court's views ought to be apparent from Part I *supra*.

[199] NET maintains that all necessary modifications could be completed within five years, but Maine's observation that some localities may require less time and others more is sound. NET should submit a detailed request for exemptions to the state regulators and to the Department of Justice.

2. *Worcester*

NET has drawn a separate Central Massachusetts LATA in conformity with the Court's April 20, 1983, Opinion, separating Worcester and its surrounding communities from the Boston area and creating a total of three LATAs in Massachusetts, but at the same time it has asked the Court to reconsider whether this third Massachusetts LATA is in the public interest. NET contends that the establishment of a third LATA will prove costly to local ratepayers; will disrupt service in nine towns divided by the new LATA boundary;[200] will decrease the validity of various optional intrastate billing plans which depend upon volume and distance;[201] and may preclude use of a No. 4ESS switch as an access tandem to the possible detriment of AT&T's interexchange competitors. The Massachusetts Department of Public Utilities also urges the Court to reconsider the division of the Eastern Massachusetts LATA into an Eastern and a Central LATA, arguing additionally that the growth of the high technology industry beyond suburban Boston westward toward Worcester has created a single community of interest in central and eastern Massachusetts. The Department of Justice, on the other hand, continues to maintain that the contribution three LATAs would make to a competitive telecommunications environment in Massachusetts outweighs the inconvenience and cost involved in the creation of a third LATA.

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[200] A larger number of municipalities would be divided, but in all but nine communities EAS routes would enable NET to continue to carry traffic across the border from one side of town to the other.

[201] This factor alone is not significant since it may be expected that interexchange competitors will respond to consumer demand for special billing plans, *e.g.*, for reduced rates on frequently called routes, in substitution or in addition to those offered by the local monopolist.

The Court has carefully reviewed the filings addressed to eastern Massachusetts, and it has decided to grant the request of NET for a single LATA for that area. Although NET continues to overestimate the cost to ratepayers of separating the LATA,[202] the other grounds it advances are persuasive. In its most recent filing, NET describes in considerable detail the impact on subscribers whose towns would be split by the new border between the Eastern and Central LATAs. The Court has also been persuaded by the NET and the PUC submissions that the population of this area is sufficiently concentrated and the local telephone network sufficiently integrated that the expense, effort, and customer inconvenience associated with dividing the network would be very substantial, even if NET's estimate of the expense is somewhat exaggerated.[203]

The detail provided by New England Telephone in its May 5 and May 23, 1983, submissions stands in stark contrast to the paucity of supporting documentation in the Department of Justice's filing. The Department offers only its bare conclusion that "the competitive

[202] Most of these costs will be reflected in interexchange carrier access charges, not in the local rate base. Moreover, these costs could be spread over a number of years.

[203] Moreover, one of the factors cutting in favor of separating the LATA—the benefit to interexchange carriers of not having to compete with the Operating Company for calls between the Worcester area and the Boston/New Bedford region—is undermined somewhat by technical access considerations which previously were not entirely clear. If Worcester is in the same LATA as Boston and New Bedford, NET will offer access to interexchange carriers by means of a No. 4ESS switch to be constructed in Framingham. If Worcester is placed in a separate Central Massachusetts LATA, two smaller switches will be built in Framingham and Worcester. NET insists that the existing cross bar switch in Worcester could not be upgraded to serve as an access tandem, and although this assertion is challenged by Southern Pacific Communications Corp., the Court is not prepared to override the Operating Company on so technical a point.

benefits of separating Worcester from Boston outweigh the costs of separation." The Department does indicate that it would consider exceptions to the new boundary to allow NET to continue to serve the divided communities, but NET persuasively counters that since calls within these municipalities are carried by the toll network—but billed as if the calls were local—"it is not clear what exemption could solve [the] problem."

The Court concludes that the palpable expense and inconvenience of separating the LATA outweigh the Department's speculation about benefits to competition,[204] and it will therefore approve the consolidation of Boston and Worcester in a single LATA.

3. *New York*

The Court accepts the Operating Company's proposal to consolidate Glens Falls and Albany into a single LATA and also to consolidate Utica and Syracuse into a single LATA.[205] To be sure, New York Telephone Co. failed to provide the Court with new information except the revised, lower count of telephones in Glens Falls,[206] but the Department of Justice has advised the Court that it

[204] Supporting the Department's position is the fact that the access provided for calls within a single LATA would not include a presubscription option while calls between Worcester and Boston, were each city in a separate LATA, would include such an option. The choice is thus between access via a No. 4ESS switch (see note 203 *supra*) and a larger area in which presubscription will not be available, on the one hand, and access via an inferior switch and greater availability or presubscription, on the other. Based on the comments the Court has received, it is reasonable to expect that the former would do more for competition than would the latter.

[205] The various requests for exceptions contained in the October 4, 1982 applications also are granted, except that New York Telephone will not be serving Wells, Vermont. See pp. 284-85 *supra*.

[206] The revised count is 97,000, as opposed to 200,000.

does not believe that the competitive purposes of the decree would be significantly advanced by creating four LATAs rather than two. In view of the Department's general tendency to err on the side of separation in close cases—as evidenced, for example, by its position on the proposed Eastern Massachusetts LATA—its failure to advocate such separation here, and the relatively small size of Utica[207] and Glens Falls, the Court is reluctant to impose on New York Telephone Co. total estimated costs of $8.6 million in network reconfiguration.[208]

4. *Pennsylvania*

Pennsylvania Bell pledges (1) to build a No. 4ESS switch in the Philadelphia LATA and lease access capacity from AT&T in the meantime, (2) to offer access in the Pittsburgh LATA through a DMS-200 switch,[209] and (3) to construct a DMS-200 switch in Harrisburg. Based upon these assurances, the Court will approve the Pennsylvania LATAs.

5. *Baltimore*

Chesapeake & Potomac Telephone Co. and the Department of Justice ask the Court to make explicit its approval of exceptions requested by C&P to allow eight exchanges in the Baltimore LATA to continue using "Metro FX" service. This service allows telephone subscribers in these exchanges to pay rates for calls to

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[207] The Utica area contains 110,000 phones, according to New York Telephone, down from the 120,000 the Company previously reported.

[208] The Court also approves the boundaries of the new Poughkeepsie LATA as proposed by New York Telephone Co.

[209] A small portion of the Pittsburgh LATA, the Greensburg area, will be accessed by a 1AESS, 2-wire machine. This is satisfactory since AT&T and its competitors will all be served by means of this switch, so that there will be no quality differences among them.

and from Washington, D. C. as if the exchanges were located in the Washington LATA. The exceptions are approved.

Some of the affected exchanges are located in Calvert County, Maryland, whose Chamber of Commerce wrote the Court in late April 1983, concerned that the County's inclusion in the Baltimore LATA would mean disruption of economically necessary discount calling into Washington. The express approval of all FX exceptions requested by C&P should alleviate the County's concerns, for in view of that approval the placement of Calvert County in the Baltimore LATA will not affect its subscribers' rates.

The Court finds, however, that the County's placement in the Baltimore LATA, as initially proposed by C&P and accepted by the Court on April 20, 1983, is reasonable in light of C&P's representation that it would cost over $3 million to reconfigure the County's local network to render it suitable for inclusion in the Washington LATA. According to C&P, this also would "leave idle about $500,000 in facility capacity between these exchanges and Annapolis," Annapolis being the location of the toll center which connects Calvert County exchanges to the long distance network.

6. *Winchester*

For the reasons stated in the Department of Justice's filing,[210] the Court reconsiders the consolidation of the

[210] The Department informs the Court that South Central Bell and GTE agree to an association of GTE's Lexington 264,864 main stations and South Central Bell's 165,000 Winchester stations. This association will ensure that the Winchester area will be attractive to interexchange carriers—the primary concern that prompted the Court to require the consolidation of the Winchester and Louisville LATAs. The Louisville LATA has more than enough stations—430,000—to enable it to stand on its own.

proposed Winchester and Louisville LATAs; approves the Louisville LATA as originally proposed; and approves the association of the Winchester LATA with the independent area around Lexington served by GTE.

7. *Birmingham/Huntsville*

South Central Bell's division of the Birmingham LATA into two separate LATAs, as required by the Court's April 20, 1983, Opinion, is approved.

8. *Midwest*

The Court approves the inclusion of Kankakee in the Chicago LATA;[211] the Detroit LATA as proposed;[212] the Grand Rapids LATA;[213] the inclusion of Sikestown and Cape Girardeau in the St. Louis LATA;[214] the borders between the Cleveland and Akron-Canton LATAs;[215] the Southeast, Wisconsin LATA as proposed;[216] and the division of the Davenport LATA.[217]

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[211] The Court accepts the reasons for this action provided by Illinois Bell, the Illinois Commerce Commission, and the Department of Justice.

[212] The Court agrees in this regard with the reasoning of the Michigan Telephone Company, the Michigan Public Service Commission, the State of Michigan, and the Department of Justice.

[213] This approval is granted for the reasons stated in the Court's April 20 Opinion and the filing of the Department of Justice. The approval is conditioned, however, upon Michigan's undertaking to implement its plans to have certain Michigan Bell exchanges home on the new GTE Three Rivers switch.

[214] This approval is in accordance with the recommendations of Southwestern Bell and the Department of Justice.

[215] This division was required by the Court's April 20 Opinion.

[216] The Court accepts the reasoning of the Wisconsin Telephone Company.

[217] This division was likewise required by the April 20 Opinion.

9. *Minnesota*

Northwestern Bell and the Minnesota Public Utilities Commission request the Court to consolidate the Fargo (North Dakota) and Brainerd (Minnesota) LATAs. The LATAs are now separated by the North Dakota/Minnesota border. Previously the Commission and the Operating Company had been at odds over five communities on the Minnesota side of the border which Northwestern Bell desired to place in the Fargo LATA rather than the Brainerd LATA.

The requested consolidation will be approved. Although it requires an exception to the decree's presumption against LATAs that cross state lines, it will accomplish the Minnesota Public Utilities Commission's objective of ensuring a LATA of adequate population to be attractive to interexchange carriers without requiring Northwestern Bell to incur $9 million in network reconfiguration costs, as would the previous proposal of the Minnesota regulators.[218] The resulting LATA would be of moderate size—216,000 subscribers not including those of Independent companies—and it would be consistent with the community of interest that spans the Minnesota/North Dakota border.

10. *Seattle*

The Court approves the inclusion of Bellingham in the Seattle LATA for the reasons stated in the May 5, 1983,

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[218] Northwestern Bell currently serves the five Minnesota border communities from facilities located in North Dakota. Under the previous proposal of the Minnesota Public Utilities Commission, the communities would have been included in the Brainerd LATA, obliging Northwestern Bell to rewire the communities to facilities on the Minnesota side of the border.

filing of Pacific Northwest Bell,[219] and since leasing space on AT&T's No. 4ESS switch would cost the Operating Company approximately $1.2 million more than installing a switch of its own, the Court approves Pacific Northwest Bell's request to provide access in the Seattle LATA through a new 4-wire digital switch.

11. *Oregon*

Pacific Northwest Bell requests the Court to reconsider its decision to require the establishment of the two LATAs initially proposed for Oregon, and to allow instead a single LATA for the entire state. The State, through its Governor, endorses the request, as does the Oregon Public Utility Commission. Pacific Northwest Bell explains its change of position as having resulted from a realization that it had proposed two LATAs based on a "conservative" reading of the decree's requirements. The Department of Justice maintains that a single LATA in Oregon would be unreasonable, and the Court agrees. Because of the distance between Eugene and Portland, the two major cities in Oregon, two LATAs configured around these cities are clearly warranted under the general standards applicable to the entire country, and the Court will not reverse its earlier determination.

12. *California*

The Court approves a tenth LATA in California composed of San Luis Obispo County as a reasonable response to its order of April 20, 1983 that the County's exchanges not be included in the Los Angeles LATA.

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[219] The Department of Justice has withdrawn the reservations it initially expressed over inclusion of the Bellingham area in the Seattle LATA, noting that although the independently served expanse between Bellingham and Seattle is large geographically, it contains only about 20,000 subscribers.

jurisdiction of the Federal Communications Commission.[220] Furthermore, if the corridor areas were configured into separate LATAs, this would force a reassessment of a number of other LATA boundaries, such as those between Long Island and New York City and New York City and Westchester, or else hugh New York-New Jersey and Philadelphia-New Jersey-Delaware LATAs would have to be established—both undesirable developments.

For these reasons, the Court approves the two proposed corridors subject to the equal access provisions discussed *infra*.

B. Intra-LATA Equal Access

With the exception of the New York and Pennsylvania corridors, the Court accepts as reasonable the commitments made by a[ll] of the Operating Companies as required by the April 20, 1983, Opinion (1983-1 Trade Cas. ¶65,333 at 69,980) to provide equal access for intra-LATA service.

First. Pursuant to the Operating Company commitments, the access offered to interexchange carriers for intra-LATA toll calls[221] will be equal in technical quality to the access provided to these carriers for inter-LATA calls, meaning that both types of access connections will be performed by the same exchange access facilities (be they access tandems or direct trunks between end offices and interexchange carrier points of presence). The access will be equal also in another respect: subscribers of AT&T and its interexchange competitors alike will not be able to select in advance either

[220] Moreover, to the extent that the rates are set above cost, the presence of competitors in the corridors will exert pressure on the Operating Companies and the FCC to reduce the price of corridor service.

[221] The intra-LATA equal access requirement does not apply to non-toll calls.

Florida, where the Public Utilities Commission has sanctioned intrastate competition by granting Microtel a license,[226] the Commission might well decide that intra-LATA competition should be further encouraged by requiring access codes alike for the Operating Company and its competitors, but the Court should not force this outcome. With respect to a state where the future of intra-LATA competition is more uncertain than in Florida, the Court would be even less justified in ordering the Operating Company to make intra-LATA telephone calling inconvenient for everyone—by adding four more digits to every intra-LATA toll call—for only speculative offsetting gains. Such a decision ought to be reserved for the state regulators, as several of them have urged.[227]

The unevenness resulting from the Court's decision between the Operating Companies and their competitors does not offend the competitive principles of the decree.

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[226] The Commission has under review whether also to license MCI for intrastate telecommunications traffic.

[227] See, *e.g.*, Comments of Maine. The situation may well be different with respect to undesignated inter-LATA calls. It would seem to be inconsistent with the decree for AT&T automatically to receive inter-LATA calls dialed either mistakenly or ignorantly without an access code (for those calls not dialed pursuant to a presubscription). The Operating Companies in that event would have two options: they could prevent an undesignated inter-LATA call from being completed (by obliging the caller to dial again using a proper access code) or to allocate undesignated calls among all interexchange carriers on the basis of some formula. This subject is not dealt with at all in the plan of reorganization; moreover, the Operating Companies have not yet formulated their own policies, and they have not advised the Court as to the practical implications of various options. The Court will therefore defer a decision on this subject. If the Operating Companies should improperly discriminate among carriers with respect to undesignated calls, remedies will be available through the Department of Justice and the Court.

the Operating Companies will have to offer complete inter-LATA access to competitors which carry inter-LATA traffic within the corridors,[229] with all that this implies, including the option of presubscription,[230] and all calls must be designated. The Operating Companies may choose whether they will develop the software that will allow separate presubscription of an intra-LATA carrier, or whether they will offer presubscription to one carrier only.

C. Bell-Independent Traffic

On February 17, 1983, the Operating Companies[231] submitted their proposed classifications of traffic between areas they serve and those served by independent telephone companies (Independents)[232] as either inter-LATA or intra-LATA.

[229] As evident from the filings, the Operating Companies intend to charge competitors inter-LATA access tariffs even though they would not be receiving inter-LATA-type access.

[230] In the case of the corridors, it is appropriate that the Operating Companies undertake the responsibility for advertising what they claim to be their less expensive, exceptional service and instructing business and residential users on how to take advantage of it. Since many of the users of these routes are businesses, which may be expected to be very cost conscious, the Operating Companies should presumably have little trouble in inducing them to dial four additional numbers (in the event that, as many assume, that Operating Company will not be the one preselected by the user) if that would save them money.

[231] AT&T states that the Operating Companies alone classified the traffic between their respective LATAs and adjacent independent territories, without interference from AT&T. AT&T Response to Comments, March 25, 1983, at 5 n.**.

[232] There are some 1425 independent telephone companies which provide local phone service in 11,000 of the 18,000 local exchanges in the United States. Objections of the United States Independent Telephone Assoc., March 15, 1983, at 2. The geographic areas where the Independents provide service are, in total, larger than those where the Bell Operating Companies provide local service; although the Independent territories are generally more sparsely populated, encompassing only 20 percent of the telephones in the nation.

13. *Pennsylvania-New York-New Jersey Corridors*

The Court gave tentative approval to two unique serving arrangements for metropolitan regions which cross state lines—the "limited corridors" running from New York City into five northern New Jersey counties and from Philadelphia into three southern New Jersey counties.

In response to questions posed by the Court, the Operating Companies and the Department of Justice provided additional information about the setting of access charges and customer rates with respect to corridor traffic. Some of the potential competitors of the Operating Companies object to the local companies' plans not to pass on to their end user customers the costs of facilities they do not use in serving them, that is, the costs of the circuits used to connect competitors' points of presence to the local loops. In the case of the corridors, which were sanctioned specifically to preserve for interstate callers in these areas the advantages of the existing local networks, the Operating Companies' policy is reasonable. As New Jersey and Pennsylvania Bell observed, "[t]o do otherwise would require the Operating Companies to compete on the basis of their competitors' costs rather than their own."

The International Communications Association registers a different complaint about the corridors. Rather than to ask for more competition within the corridors, it wants to ensure that the Operating Companies' efficiencies will be passed on to consumers in the lowest rates possible, and it argues that this would more assuredly be accomplished if the corridor areas became LATAs (so that all traffic within a corridor would be intra-LATA). It is difficult to understand what difference this would make since the area would still be interstate and the rates would therefore still be subject to the

AT&T or one of its competitors as a transporter of intra-LATA toll calls—the so-called "presubscription" or "preselection" option. Rather, if a subscriber wishes to place an intra-LATA call through AT&T, MCI, Sprint, Microtel, or one of the other competitive services, he will have to add four digits at the time of dialing (*i.e.*, an access code of "10XX"). If any access code is not dialed, the intra-LATA call will automatically be carried by the Operating Company.

What that means, of course, is that, with respect to intra-LATA traffic, there will be inequalities between all interexchange carriers, on the one hand, and the Operating Companies, on the other. Telephone users will be able to access an Operating Company as they do now, simply by dialing a seven or ten-digit number (depending upon whether an area code is used).[222] To access an interexchange carrier, on the other hand, a telephone user would consciously have to select that carrier and dial the appropriate four-digit access code. Additionally, the Operating Companies (with their proliferation of direct trunks between Class 5 end offices and the concomitant ability to transport calls without the need for switching) may be able to carry their intra-LATA toll calls with higher quality and at less cost than can the competitors carry theirs.

A number of interexchange carriers attack this scheme both on account of the absence, to them, of the presubscription option, and because of the inequalities in facilities between the Operating Companies and their potential intra-LATA toll competitors.

The Court has concluded that, in light of all the circumstances and competing considerations, the position of the Operating Companies is not unreasonable. In ap-

[222] The latter would also have to be accompanied by a prefix "1" in those areas where an area code must be distinguished from a local exchange code.

proving the consent decree as in the public interest, and in directing the Operating Companies to provide intra-LATA access, it was not the Court's intention to require the decimation of the local telephone networks or to deprive customers of the conveniences and cost benefits which the Operating Companies have succeeded in making available to them.

It would cost approximately $1 billion and take several years to modify the 3,000 Bell end offices so as to permit a telephone user to presubscribe for one carrier for intra-LATA toll calls and another carrier for inter-LATA calls.[223] In the absence of such an expenditure—which the Court will not require—what will be available to the customer in the near future is the option to preselect one telephone company, and one only. If such a customer could select in advance either an interexchange carrier or an Operating Company for intra-LATA calls, many, if not most, telephone users would preselect the former rather than the latter. This is so because of the overriding fact that, under the decree and the plan of reorganization, the interexchange carriers are allowed to carry all toll calls (both inter-LATA and intra-LATA) while the Operating Companies may carry only intra-LATA calls—a significant drawback with respect to convenience. Thus, to require the Operating Companies to provide the presubscription option to the interexchange carriers would place the local companies at an almost insuperable disadvantage. This the Court will not do.

Even if a subscriber cannot or does not presubscribe, he may still designate a particular carrier at the time he makes the actual call (by dialing a specified access code).

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[223] This is because the end office would require revised computer software that could determine when a call was designated for a termination point within its LATA and when it was destined for a point in another LATA.

What if a customer does not do so—which carrier will get that business? Some suggest that all intra-LATA toll calls should be required to be designated.[224] That, too, will not be required.

To require all callers to use a four-digit access code, in addition to the number to be called, for all intra-LATA toll calls—including those carried by the local Operating Company—would have the perverse consequence of making intra-LATA, or local toll calls more cumbersome to dial than inter-LATA, or long distance toll calls.[225] This is totally inappropriate. The alternative—which the Court will allow—is to route all undesignated intra-LATA toll calls to the Operating Company.

This conclusion is buttressed by the consideration that affirmatively to forbid such an arrangement would inappropriately override state regulators' authority to decide what intrastate calling arrangements are best suited to the public interest within their states. In a state such as

[224] Microtel, Inc. argues that

> with equal access should come a more uniform starting point for intra-LATA competition. We have no illusion that the BOCs will not continue to enjoy significant competitive advantages arising from their historical relationship with customers and their dominant position in the . . . market. But those advantages should not be solidified by an additional head start arising from carriage of undesignated intra-LATA traffic.

Opposition dated May 16, 1983, at 14. There is some merit to that argument, particularly in states where the Court approved large LATAs on the expectation that there would not be significant barriers to intra-LATA competition. Microtel's primary state of operation, Florida, is a case in point. The Court allowed the consolidation of three SMSAs to form the Southeast LATA (Miami, West Palm Beach, and Ft. Pierce) with the understanding that there would be intra-LATA competition for calls between these cities.

[225] Due to the availability of presubscription in inter-LATA calls, someone who had preselected an interexchange carrier would not have to dial an access code and he therefore could dial across the country with fewer digits than within his own LATA.

The decree mandates that the Operating Companies have primary responsibility for exchange services, and it is appropriate therefore that they should enjoy the non-access code arrangements with their exchange customers. The competitors are merely secondary suppliers of intra-LATA service, and while they may operate in that market on that basis, they should hardly be given what in view of the considerations discussed above, would amount to a preferred position. However, if they should truly offer a better price or a better service than the Operating Companies, they should be able to educate their potential customers that it is worth the extra four numbers to take advantage of their offering.

Second. The reverse is true with respect to the so-called corridors.[228] These corridors traverse not only LATA boundaries but also state boundaries, and they thus represent dual exceptions to the decree. They were permitted by the Court in heavily populated metropolitan areas not out of a desire to "[maintain] the position of the Operating Companies in the corridor," as New Jersey Bell and the Bell Telephone Company of Pennsylvania assert, but to maintain for consumers the benefits of what were represented to the Court to be particularly efficient network arrangements.

The decree presumes that the interexchange carriers—not the Operating Companies—will be the primary transporters of interstate, inter-LATA telecommunications. One of the reasons underlying the Court's tentative approval of the corridors—which would allow the Operating Companies, too, to operate in the markets the corridors represent—was that these routes would be fully open to competition. To implement that purpose,

[228] The corridors, as indicated at pp. 294-95 *supra*, run from the five boroughs of New York City into five northern New Jersey counties, and between five Eastern Pennsylvania counties into three southern New Jersey counties.

The need for such a process came about because of the proximity of many Bell and Independent areas, and the consequent joint Operating Company/Independent service arrangements which are currently in effect around the country (that is, the Operating Company typically switches traffic between its end offices and the offices of the Independent, which then routes that traffic to its final destination). If all that traffic were considered to be inter-LATA under the decree, the Operating Companies would be prohibited from participating in such arrangements, and significant, costly network rearrangement would have to be undertaken in order to have all Bell-Independent traffic carried by an interexchange carrier.[233] To avoid such disruptive effects, the Operating Companies were asked to identify those areas where, consistent with the decree's purpose of limiting Operating Company participation in the long distance competitive markets, they should nevertheless be permitted to continue to provide joint service offerings with adjacent independent companies.[234] In addition to determining whether the particular Operating Company may carry such traffic or whether it should be precluded from doing so, the classifications will also be the basis for deciding whether Bell System facilities and assets connecting Bell and Independent territory should be assigned to AT&T or to an Operating Company.

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[233] This would be so even where highly integrated communities are involved.

[234] Under the terminology used by the parties, if a particular Independent territory is considered to be "associated" with the adjacent Operating Company LATA, then telecommunications traffic between these two areas is regarded as intra-LATA and may be handled by the Operating Company. If, on the other hand, a particular Independent territory is considered to be "not associated" with an Operating Company LATA, then the Operating Company would be prohibited under section II(D) of the decree from carrying traffic between the two areas, as this would be regarded as an inter-LATA service.

On February 23, 1983, the Court issued an order establishing procedures for the review of the classifications prepared by the Operating Companies. Subsequently, a number of interested parties submitted comments, and AT&T and the Department of Justice filed their own responses.

The classifications, although made by the Operating Companies, are based upon principles and criteria furnished to these companies by the Department of Justice. The fundamental governing principle used by the Department and hence by the Operating Companies was that, for the purpose of determining whether the traffic between an Operating Company and adjacent Independent territory is to be regarded as inter-LATA or intra-LATA, Independent territory was treated as if it were Bell territory. Traffic is thus classified as intra-LATA if it would have been included within a LATA had it been exclusively Bell territory; it is classified as inter-LATA if it would have required the establishment of a separate LATA.

On November 17, 1982, the Department of Justice set forth the criteria by which it would judge the Operating Company determinations.[235] The following types of Bell-Independent traffic were designated as clearly intra-LATA:

> (1) traffic within local calling areas and non-optional extended area service (EAS) areas;
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> (2) intrastate traffic for states with a single LATA;
>
> (3) traffic within a single statistical area; and
>
> (4) traffic between a LATA and Independent exchanges serving non-statistical areas.

[235] Letter from James P. Denvir to Jim G. Kilpatric, November 17, 1982, at 3-7.

The following types of Bell-Independent traffic were designated by the Department as "possibly" intra-LATA:

> (1) traffic between a LATA and Independent territory in an adjacent SMSA which includes fewer than 100,000 main or equivalent main stations, or the distance between the core cities of the two areas is less than 25 miles;
>
> (2) traffic between a LATA and Independent territory without a Class 4 switch (or other network considerations); and
>
> (3) traffic between isolated Bell exchanges and an Independent dominated SMSA, provided that the Independent makes a commitment to provide equal access.

The remaining traffic is regarded under the criteria as inter-LATA.

Reliance upon these criteria by the Department, and hence the Operating Companies, would have the following impact in the two factual circumstances which are predominant with respect to Bell-Independent traffic: (1) an Operating Company LATA may not be associated with an Independent area if the latter constitutes a market of sufficient size and distance from other markets to attract multiple interexchange carrier entry; (2) if, to the contrary, the Independent area has relatively few access lines or if the distance between the Bell and Independent core communities is insubstantial, an association between the Operating Company LATA and the Independent area will be permitted. In a few instances, particularly in Oregon and Washington, traffic was classified as inter-LATA by the particular Operating Company because it elected not to serve the relatively small Independent area in question.[236] In a number of

[236] The Department of Justice as well as the states involved oppose these classifications on the ground that even though the decree cannot impose a requirement that an Operating Company actually pro-

other instances, where the Operating Companies and the Independents agreed that there will be no Operating Company service despite an absence of a prohibition in the decree, the traffic was also classified as inter-LATA for purposes of the division of Bell System facilities.[237]

The two principal objections[238] which have been advanced with respect to the Bell-Independent traffic

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vide service to an area which it is permitted to serve, the purpose of the classifications is to define areas which the Operating Companies *may* serve. In that view, the particular traffic should be classified as intra-LATA and it would then be left to the state and federal regulators to determine whether the Operating Companies or any other carriers should be *obligated* to serve particular areas. See Department of Justice Response to Comments, April 4, 1983, at 8; State of Oregon Comments, March 15, 1983, at 3-5. The Court finds the position taken by the Department of Justice in this regard to be correct, since it will best ensure that the decree does not unnecessarily intrude upon the jurisdiction of the regulatory commissions to determine service responsibilities within their jurisdictions. Accordingly, the Operating Company classifications are hereby required to be modified to conform to the Department's position.

[237] However, for the purpose of determining whether the Operating Company may serve these areas, the traffic between the two areas will be classified as intra-LATA. Thus, if in the future an Operating Company wishes to provide service to such Independent areas, it will be free to do so. This minor category of classifications is, in essence, simply a request by the particular Operating Company for an exception to the general rule that it be assigned Bell System Facilities devoted to intra-LATA service. Instead, AT&T will be assigned these facilities which the Operating Companies do not intend to use. See Department of Justice Response to Comments, April 4, 1983, at 9-10. No objections have been raised with respect to this exception to the general rule for the division of Bell System assets, and it is, therefore, approved.

[238] It has also been argued that the Court should require that an opportunity be afforded the intervenors to seek reclassification of Bell-Independent traffic after divestiture. There is no basis for such a request, and it will be denied along with all other demands for systematic post-divestiture proceedings. See Part IX *infra*. However, the Bell Operating Companies may, under the decree, subsequently petition the Court for reclassification or for exceptions in regard to service between their own areas and Independent territory.

classifications are first, that in certain instances either too many or too few Independent areas have been associated with Operating Company LATAs; and second, that the classifications unduly curtail the business freedom of the Independents.

First. The Court has considered the various Bell-Independent traffic classifications on the same basis as its earlier consideration of the LATAs.[239] Although it is possible to disagree with particular decisions that were made by AT&T and the Department of Justice in this process, the Court has concluded that in no instance have the intervenors made a case sufficiently compelling that it calls for a rejection of the classification.[240] The Department's guidelines are reasonable and consistent with the principles of the decree, and these guidelines were properly applied by the Operating Companies.[241]

Second. The "business freedom" claim is largely based upon a misunderstanding concerning the substantive scope of the classification decisions. Contrary to the assumption of some intervenors, the classification of par-

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[239] It is questionable whether, in view of the relatively limited impact of these classifications upon the intervenors (see *infra*), a level of scrutiny comparable to that employed with respect to the LATA classifications themselves was required.

[240] No objections were raised to the vast majority of Independent exchanges that have been classified as "associated." It is to be noted that only 940 out of the 11,000 Independent exchanges are classified as "not associated" to any Bell Operating Company LATA. Objections of the United States Independent Telephone Assoc., March 15, 1983, at 4 n.*.

[241] In the few instances, such as those discussed in note 236 *supra*, where the Department of Justice and the Operating Companies took different positions with respect to whether particular traffic should be classified as intra-LATA or inter-LATA, the Court agrees with the position of the Department, and the classifications should, accordingly, be modified to conform to that position.

ticular traffic as intra-LATA does not have as its consequence that interexchange carriers may not offer service with respect thereto or that the Independents may not directly provide access arrangements to these carriers.[242] The intra-LATA or inter-LATA classifications—in this context as in the context of service within the Bell territories—bind only the Operating Companies and affect only their ability to provide service; they do not bind the interexchange carriers or the Independents and they will not in any way affect their ability to provide service.

To be sure, where traffic has been classified as inter-LATA, an Operating Company may not be "associated" with the adjacent Independent territory, and to that extent it may be said that the business freedom of the Independents is being restricted.[243] That, however, is an in-

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[242] Several intervenors argue that, although the associations being decided now have limited purposes under the decree, they will be "frozen in time" for state and federal regulatory bodies, common carriers, Independents, and ratepayers. See GTE Comments of March 15, 1983, at 3. There is nothing in the plan of reorganization which the Court is approving which has such wide consequences. If others decide to accept the decisions made herein, that would be their decision; it can hardly be a basis upon which the Court would be justified in rejecting the plan. Nothing in the Court's approval of the Bell-Independent classifications is intended in any way to restrict the regulatory bodies in the exercise of their legitimate authority.

[243] Moreover, regardless whether traffic is classified as intra-LATA or inter-LATA, Independents will have the option of establishing a relationship with an Operating Company whereby the Independent would be the carrier of traffic between its territory and the Operating Company LATA. See 1983-1 Trade Cas. ¶65,333, at 69,982-83. If the Independent does not wish to carry such traffic itself, it will alternatively be able to enter into a service arrangement with AT&T (in which case it could continue to interconnect with the same Bell System facilities as are presently used for its interexchange of traffic with Bell territory) or any other interexchange carrier. AT&T Response to Comments, March 25, 1983, at 12.

evitable consequence of the decree which limits the Bell Operating Companies to intra-LATA service; it cannot be regarded as a defect in the classifications made by the Operating Companies and approved by the Department of Justice. The objections to these classifications, as well as to the classification process, will accordingly be rejected.[244]

The proposed Bell-Independent classifications will be approved.

## VIII

### Central Staff Organization

Section I(B) of the decree requires the creation of a central organization jointly funded and utilized by the Regional Companies (1) for the purpose of meeting national security and emergency preparedness requirements and (2) for administering such functions and services as can most efficiently be performed on a centralized basis.[245] Pursuant to these provisions, AT&T has proposed, and the Department of Justice has approved, the creation of an 8,800-person Central Staff Organization (CSO) which would engage in a number of technical and nontechnical functions[246] to replace support which the

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[244] Similarly, GTE's complaints regarding splintering of trunk groups, duplication of facilities, and stranding of existing facilities are basically inevitable consequences of the decree insofar as it does not permit the Bell Operating Companies to carry interexchange traffic.

[245] Section I(A)(1) permits AT&T to transfer resources to such an entity.

[246] Of the total 8,800, approximately 6,600 staff members would perform technical functions. Plan of Reorganization at 239.

Operating Companies have until now received from the AT&T General Departments, Bell Laboratories, and Western Electric.[247]

A. CSO Responsibilities

Under the plan of reorganization, the CSO will perform technical services to support the Operating Companies in the "construction, operation, and maintenance of their local exchange networks."[248] AT&T has listed five such technical functions:

(1) network planning, which is described as "a long-range function concerned with recommending to the BOCs the optimal direction in which the local networks should evolve";[249] (2) systems engineering, that is, the development of "generic requirements for new systems" which will enable the Operating Companies to "inform vendors of the features and functions that the BOCs want or need in the equipment they purchase"; (3) applied engineering, that is, the testing and evaluation of the products of potential suppliers to determine whether they meet the generic requirements developed by the systems engineers; (4) applied research, involving "state-of-the-art research in switching, signaling, materials and other elements which provide the underpinning for exchange telecommunications"; and (5) information systems support, which will involve "maintaining and enhancing a number of computer-based operations and administrative systems integral to the exchange business."[250]

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[247] The employees would be tranferred from AT&T and its affiliates, transferred from the Operating Companies, or newly hired.

[248] AT&T Response to Objections at 505.

[249] The network planning group within the CSO will also recommend internal network requirements and technical interface standards.

[250] AT&T Response to Objections at 506-12.

Among the non-technical functions will be the provision to the Operating Companies of procurement support services,[251] and such other assistance as legal services, [252] regulatory support services, marketing (including billing and sales support) services, financial services, human resources development, and employee relations.

The criticisms leveled at the CSO proposal fall essentially into two categories.[253] First, intervenors representing regulatory and consumer interests contend that AT&T has presented inadequate justification for what is contended to be an overly large and costly organization. Second, potential equipment suppliers of the Operating Companies claim that the CSO may, in effect, exercise control over many procurement decisions, discriminate in favor of Western Electric products, and, over time, become a second-generation AT&T. After careful con-

[251] There would be 700 procurement support personnel. Plan of Reorganization at 339. The Court expects that this staff will not make substantive procurement decisions.

[252] The Court has some concern that the centralized provision of legal advice on potential antitrust liability might be of questionable propriety and wisdom. William Weiss, designated chief executive of the Midwest Region, testified at the June 2, 1983 hearing that: "I cannot conceive of a corporation the size of mine in the future not wanting to be self-sufficient in areas of liability like antitrust . . . ." Transcript at 25497. Although this is not a complete answer, the likelihood of antitrust violations through the central legal staff is not sufficiently substantial that elimination of these functions will be required.

[253] The delegation of national security and emergency responsibilities to the CSO is largely unchallenged. The Court has always insisted that legitimate Department of Defense interests be fully protected (552 F. Supp. at 208-209), and the CSO provisions of the plan carry out that objective. The security and emergency responsibilities will be executed by a specialized group within the CSO which will set and enforce technical standards to the extent that security and emergency needs demand that telephone equipment be "capable of being interconnected nationwide." Plan of Reorganization at 418-19.

sideration, the Court has concluded that these objections are not sufficiently weighty to warrant either the rejection or the modification of the CSO provisions of the plan of reorganization.

B. CSO Size

There is substantial evidence that the CSO is neither too large nor too costly a burden on the Operating Companies. Since these companies will be controlling the CSO—not the other way around—and since most of the costs of the CSO will not be capable of capitalization, the local companies will have strong incentives to avoid wastefulness in the CSO's operation.[254] In fact, it appears that the total cost of the CSO to the Operating Companies will be considerably less than what they now pay to AT&T for centralized support.[255]

Moreover, and significantly, the chief executives of the Regional Companies, who played an active part in molding the CSO,[256] have given an exceptionally strong

[254] Several intervenors complain that the plan makes insufficient provision for an Operating Company's withdrawal from the CSO. Complete withdrawal may only take place with five years' advance notice, and an Operating Company may withdraw from a particular function on one year's notice. The chief executives of the Regional Companies support this approach as necessary to ensure the continuing viability of the CSO, and the Court sees no reason to interfere with their judgment.

[255] William Weiss stated that the amount will be three-quarters of the sums previously expended (transcript at 25,500), while AT&T claims that the 8,800 CSO employees should be compared to the 23,000 AT&T employees allegedly now supporting the Operating Companies. Response to Objections at 496 note **.

[256] A task force of Operating Company presidents initially recommended the structure of the CSO. Each regional planner on the task force then conferred with his respective chief executive officer, and a "CSO package" was adopted by these officials in October 1982. Since that time, some functions have been added and others eliminated, and negotiations over the CSO's final form are continuing, without the participation of AT&T. Response to the Operating Companies in the

endorsement to the size of the organization, its cost, and the responsibilities vested in it by the plan of reorganization.[257] In short, the concern of some of the intervenors that the CSO is an AT&T tool designed to hamper Operating Company progress rather than to assist these companies is not shared by those most directly involved.[258] On this issue, at least, the opinions of the Regional Company managers are entitled to more weight than those of regulators[259] and consumer groups.

Some of the intervenors also question the assignment to the CSO of functions other than those strictly related to national security and emergency preparedness. The decree permits the CSO to perform such functions as "can most efficiently be provided on a centralized basis." Section I(B). It appears obvious that, with respect to the responsibilities which are vested in the CSO by the plan of reorganization, substantial economies will be realized

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Mountain-Northwest Region, May 31, 1983, at 5; Southeast Region's Response, May 31, 1983, at 3. According to William Weiss, "the presidents . . . elected to do only certain things in the central staff, those things that they felt could be done to achieve economies of scale. They excluded from the role of that central staff things that they felt either we could do ourselves with our present organizations and the Operating Companies or that didn't need to be done in the longer term future." Transcript at 25500.

[257] See, *e.g.*, Response of Operating Companies in the Mountain-Northwest Region, May 31, 1983; Response of the Northeast Region, May 31, 1983; Response of the Mid-Atlantic Bell Telephone Companies, May 31, 1983; Southwest Region's Response, May 31, 1983.

[258] The Court has no question that on this subject the chief executives of the Regional Companies communicated to the Court their genuine convictions.

[259] Some of the state regulatory commissions complain that they will be unable to exercise effective control over the costs of the CSO, but this was refuted by testimony at the June 2, 1983, hearing to the effect that the Operating Companies will present their respective shares of the cost of the CSO to the state regulators, so that "[i]t will not escape [their] attention." Transcript at 25,501.

from centralization. To be sure, AT&T has not provided a quantification of efficiencies and economies, but that is not especially surprising since it is unlikely that detailed cost-benefit comparisons could now be made: the seven Regional Companies are at present only planning to operate in this respect, and the territory is somewhat unchartered. It does not require an army of efficiency experts, however, to conclude that it will be more economical for certain support functions to be performed once rather than seven times over. As the Department of Justice has aptly observed, "it is neither necessary nor useful to engage in extensive second-guessing of the [Operating Companies'] decisions as to what activities can efficiently be centralized."[260]

The Court concludes that the objections regarding size, scope, and cost of the CSO do not warrant disturbing the CSO proposal.

C. Procurement Functions

The objections relating to the CSO's possible involvement in procurement activities have somewhat more substance. The intervenors complain in this respect primarily that standards may be set by the CSO which will favor Western Electric products over those of competitors, and that the testing of products may be biased against Western's competitors.

It seems beyond debate that uniform standards are necessary to ensure high quality in the telephone system, indeed its very survival as a nationwide network.[261] Nor are such standards incompatible with competition. Not all characteristics of products to be purchased by the

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[260] Department of Justice Response to Comments at 162.

[261] There are some features, *e.g.*, network signaling protocols, which will be of no use unless they are agreed to by all the Operating Companies. AT&T Response to Objections at 523.

Operating Companies will be specified in advance; there will be ample room for competitors to meet the generic requirements established by the CSO and still produce products drawing upon their special skills, distinctive styles, and other competitive advantages.

Similar conclusions apply to the testing function to be performed by CSO personnel. AT&T has advised the Court that such personnel will not make product recommendations to individual Operating Companies but will limit themselves to "a scientific and objective testing function." Test results will be made available to both the Operating Companies and the manufacturers, and the latter will be allowed an opportunity to demonstrate the incorrectness of any adverse findings. And it will be up to the Operating Companies, not the CSO, to determine the weight and significance to be accorded to the test results in the making of final procurement decisions.[262] The Court believes that these assurances adequately protect potential vendors.[263]

Some intervenors question more broadly whether objective conclusions are at all possible with respect to such activities as standard-setting, testing, and the like,[264] and that in practice it may not be possible to distinguish sharply between these functions and procurement decision-making. Another intervenor asks who at the Operating Company level would "undertake an independent and intelligent analysis of the technical and other evaluations sent to [these companies] by the CSO"

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[262] AT&T Response to Objections at 525-26.

[263] Should it ultimately appear that the CSO deviates from these standards, there will be time enough for the Department of Justice, the Court, or both to take corrective action.

[264] See, *e.g.*, Reply of U.S. Telecommunications Suppliers Association at 7; ITT Reply at 15.

if, as AT&T asserts, there are not enough qualified technical personnel in the Bell System to staff both the Operating Companies and the CSO.[265]

Although these objections are not without some force—particularly those related to the somewhat shadowy line between standard-setting and procurement—the Court has decided that, on balance, the advantages to be achieved from the centralization of these various responsibilities outweigh the dangers visualized by the opponents of such a step. The issue reduces itself to an inquiry whether the desirable ends of economy and uniform quality can be achieved without serious risk that the CSO will become an instrument of anticompetitive conduct. In the Court's view, that risk, *i.e.*, the risk of bad faith, is relatively small,[266] for a very basic reason.

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[265] See GTE Reply at 8.

[266] Since the representations made by AT&T in its Response to Objections regarding the limited role of the CSO in setting standards and testing products were critical in persuading the Department of Justice and the Court to approve the CSO as proposed, it is of course essential that the CSO abide by those representations. The Court has considered adopting the suggestion of some (*e.g.*, U.S. Telephone Suppliers Association) that these representations be reduced to a separate contract, but in the interest of avoiding the imposition of yet another set of rules on the Operating Companies, it will not insist on this measure. However, the Court does expect the Operating Companies to use the CSO to further only their own competitive interests, not those of AT&T, and it also expects the Department of Justice to be vigilant in its oversight of the CSO's role in the setting of standards and testing of products.

The plan of reorganization does not limit the CSO to the responsibilities initially entrusted to it. The Court is persuaded that some flexibility is necessary in this regard as well. However, here, too, it expects that the CSO will respect the boundaries between standards and testing, on the one hand, and procurement, on the other. It is in this area particularly that the Court will not hesitate to exercise the powers vested in it by section VIII(I) of the decree should this appear to be warranted.

There will be no continuing relationship between AT&T and the CSO,[267] and therefore no economic incentive for CSO personnel to favor Western Electric products over those of any other supplier. CSO personnel will, at least indirectly, be working for the Operating Companies; their success in their new employment will be bound up with the success of the local companies;[268] and the Operating Companies are far more likely to flourish by purchasing the best equipment at the best price than by favoring Western Electric products regardless of quality or price. The employees' economic incentives therefore all run in favor of the Operating Companies and against improper favoritism toward Western Electric. Moreover, the testimony of the regional chief executives and their various filings with the Court establish that they intend to make their own procurement decisions, and that they are acutely aware of the spectre of an enforcement action brought by the United States should the CSO act anticompetitively.[269]

In the absence of an economic incentive, much is made of the emotional attachment of CSO personnel to AT&T—the former employer of many of them. Such an attachment cannot be entirely discounted, at least with respect to some employees and at least in the short run. But it defies all experience with a mobile work force in the United States to assume that, for any length of time, former AT&T personnel will make decisions which will assist their former employer, but now sometime com-

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[267] Whatever sharing contracts that will be in effect will be between the Operating Companies and AT&T, not the CSO and AT&T.

[268] The CSO will not, on its own, manufacture or market any product or service.

[269] See, *e.g.*, Transcript at 25502.

petitor, simply because they used to work there.[270] Certainly the Court would not be justified in vetoing an arrangement agreed to by AT&T, the Operating Companies, and the Department of Justice which is otherwise perfectly sensible and reasonable upon the basis of so speculative an objection.[271]

The Central Staff Organization is designed to carry out extremely important responsibilities. Not only will it perform the coordination for national defense and other emergency purposes that is vital to the nation's security, but it will also set the standards which will permit telecommunications to continue to operate in an engineering sense as one national network.[272] These responsibilities were in the past performed exceedingly well by AT&T. In the Court's view, it is essential that the break-up of the Bell System and the economic competition which will result from that break-up will not lead to a departure from that high standard or to the development of balkanized regional networks which poorly interconnect with each other to the detriment of all users. The Central Staff Organization will be an important check against deterioration and fragmentation of the existing telephone system.

For these reasons, the Court is strongly committed to the success of the CSO, and it will not weaken that

[270] This conclusion would seem to hold notwithstanding the strong feelings of loyalty which have been fostered and have traditionally existed within the Bell System.

[271] As for the claim that the very establishment of a CSO might give rise to antitrust problems it is well established that a joint technical organization with responsibility for setting standards does not in and of itself violate the Sherman Act. See *American Society of Mechanical Engineers, Inc.* v. *Hydrolevel Corp.*, 456 U.S. 556 (1982).

[272] The testimony at the trial demonstrated that the application of nationwide standards has contributed substantially to the overall quality of telephone service enjoyed in this country. See, *e.g.*, testimony of Casimir Skrypczak, transcript at 23854-55.

organization, whether in size or in authorized responsibilities, without good cause. The arguments proffered by the intervenors, while they do not, here and there, lack some plausibility, are far from being sufficiently persuasive to provide such a cause. The Court accordingly will approve the Central Staff Organization as it is proposed in the plan of reorganization.

## IX

### Further Court Proceedings

Several intervenors suggest additional judicial or other proceedings of various kinds beyond those that are expressly provided for in the decree. For example, the State of New Mexico asks that the intervention status of all third parties be continued to permit them to participate in the true-up process following divestiture.[273] The State of California asserts[274] more specifically that a true-up procedure is necessary to ensure the achievement of target debt ratios, pointing out that the plan already contemplates such a procedure with respect to a number of other subjects.[275] American Satellite Company asks for the submission to the Court of detailed information concerning the day-to-day progress in the implementation of the plan of reorganization and requests public disclosure as well as judicial review of all divestiture-related con-

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[273] Reply Comments of the State of New Mexico, April 13, 1983, at 18-19.

[274] Further Comments of the People of the State of California, Feb. 14, 1983, at 65-67.

[275] These include a true-up of certain Operating Company accounts (1) to correct faulty estimates of depreciation reserves, of the assignment of assets and liabilities and of personnel assignments, (2) to correct mistaken personnel assignments and inadvertent work force imbalances, and (3) to accommodate personal hardships. Plan of reorganization at 160-62, 233-34, 277-78. See Part V(B) *supra*.

tracts.[276] And the State of Maine urges that the state and local public utilities commissions be allowed to participate in the division of assets between AT&T and the Operating Companies by a court-imposed requirement of the distribution to them of the same kinds of information and monitoring rights possessed by the Department of Justice. The Court will deny all of these and similar requests.[277]

There now is some provision in the decree, albeit on a carefully limited basis, for the retention of jurisdiction by the Court.

Section VII specifies that, upon application of a party or an Operating Company, the Court may issue orders to construe the decree, carry it out, modify it, or enforce it, or to punish violations.[278] At the request of a number of intervenors, the Court announced the adoption of a procedure which would permit an interested nonparty to initiate enforcement proceedings on its own. But that opportunity was deliberately kept very narrow[279] because, as the Court stated on August 11, 1982, so restricted it

[276] Reply Comments of American Satellite Co., April 4, 1983, at 2-4.

[277] See note 283 *infra*.

[278] The Court subsequently required the adoption of section VIII(I) which permits the Court to undertake the various section VII responsibilities (except that of modifying the decree) *sua sponte*, rather than merely upon request.

[279] Such a party may serve upon the Department of Justice a request for enforcement. If the Department refuses to take action in response thereto, an application may be made to the Court for the initiation of "further appropriate proceedings." The process was carefully restricted to complaints accompanied by affidavits alleging facts with particularity which, if true, would demonstrate a bad faith refusal by the Department to enforce the judgment. 552 F. Supp. at 220. The Court will in due course issue an implementing order, and it will not entertain enforcement requests which do not follow this route.

above, this direct oversight should end with the approval of the plan of reorganization.

To be sure, the reorganization process is not complete: the division of assets, the transfer of employees and stock, and the upgrading of the Operating Companies to the status of truly equal access providers have yet to occur. Also, as several intervenors point out, it is possible that those within the Bell complex who will actually implement the reorganization will attempt to depart from the spirit if not the letter of the decree. However, notwithstanding some failures,[281] the parties have not given evidence of bad faith sufficient to impose upon them the rather draconian requirements requested by the intervenors.[282]

There comes a time, once the basic documents have been approved, when the Court, rather than to superintend on an intensive basis the actual implementation of the reorganization, should, in the interest of keeping judicial involvement to a necessary minimum, leave com-

[281] *E.g.*, the attempts of the Department of Justice, of AT&T, or both, to disavow commitments previously made with respect to patent and trademark rights to be granted to the Operating Companies (see Parts III and IV *supra*) and the continuing reluctance of the Department to accept as final the decision regarding the marketing of CPE by the Operating Companies. See pp. 258-59 *supra*. That reluctance gives rise to some concern regarding the Department's willingness and ability to enforce fairly the CPE provisions of the decree (rather than to seek, once again, to pursue its own notions in that regard) and this, of course, casts some doubt upon the Department's overall attitude with respect to the implementation of the decree. However, in these respects, too, the various judicial powers enumerated above are adequate to deal with any recalcitrance, whatever form it may take.

[282] It should also be noted that independent auditors and actuaries will verify compliance by AT&T and the Operating Companies with the requirements of the plan of reorganization regarding the assignment of assets and liabilities. AT&T Response to Objections at 355-60.

strikes a proper balance between the need for some enforcement mechanism not under the direct control of the parties and the necessity of avoiding "constant, unnecessary interference by AT&T's competitors and others with implementation of the reorganization and with the normal operations of AT&T and the divested Operating Companies . . . [as well as the necessity not to burden the Court] with innumerable requests for clarification or modification, and with charges of violations." 552 F. Supp. at 219-20.

The Court will not expand these provisions. The difference between the procedures described above and those presently suggested by the intervenors is that the former are designed to be invoked only sporadically, upon the occurrence of some specific incident regarding the decree, while the latter would involve the Court, the intervenors, or both, on a more or less continuing basis in the divestiture process. The Court has no wish to be engaged on a long-range basis in oversight either of the divestiture or of the operations of the various components of the Bell System; such an oversight role would not be consistent with the principle of proper judicial restraint; and the kind of interference which it implies would not be fair to those who will manage AT&T and the Operating Companies.

The Tunney Act requires a court to determine whether certain consent decrees are in the public interest and, in view of the unusual circumstances of this case,[280] this responsibility also required the Court to pass upon the validity of the plan of reorganization under the decree and to allow third party intervenors to participate extensively in the review process. But for the reasons outlined

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[280] *E.g.*, the size of the divestiture, the sketchy nature of the decree itself, and, ultimately, the broad implications of the divestiture upon the entire telecommunications industry.

pliance to the managers of the business interests directly involved, with such oversight as is vested in the Department of Justice by the decree. See, *e.g.*, section VI.[283]

Should the Court's expectations with respect to the good faith and the fidelity of the parties to the letter and the spirit of the decree be disappointed with regard to any particular matter, there will be time enough under section VII, section VIII(I), and the Court's general equity powers, to take appropriate action. Except for such an eventuality, however, the Court's direct oversight role will come to an end with its approval of the plan of reorganization.

## X

## Conclusion

### A. Summary

The Tunney Act imposed upon the Court the responsibility for determining whether the consent decree submitted to it by the parties was "in the public interest." In August of 1982, the Court approved the heart of the decree—divestiture—as satisfying that standard. At the same time, it determined that its public interest responsibilities required it to pass also on the plan of

[283] For similar reasons, the Court rejects the request of the State of California that the prices charged by Western Electric be controlled for a period following divestiture (Further Comments of the People of the State of California, Feb. 4, 1983, at 41); the request of the State of Missouri to provide special representation for the Operating Companies in the form of an independent attorney (Motion of the State of Missouri for a Hold Separate Order, April 13, 1983); and the request of New York City for the appointment of a Special Master pursuant to Rule 53 (Comments of the City of New York, Feb. 14, 1983, at p. 4). Suggestions similar to these were considered and rejected by the Court prior to the entry of the decree (552 F. Supp. at 166, 220-22). No new grounds have been adduced; indeed, the Operating Companies have not been reticent in recent months to advance their views to the Court, often contradicting those of AT&T. As the Operating Companies progress further on the road to independence, they may be expected to be increasingly strong-willed in protecting their rights *vis-a-vis* AT&T.

reorganization, since that plan was to fill in the decree's many interstices and to describe the precise method by which divestiture was to be accomplished.[284] The plan was submitted by the parties, and the Court has since subjected it to thorough scrutiny, on its own and with the assistance of the parties and over one hundred intervenors.[285]

To the extent that it has been free to do so,[286] the Court, in exercising its Tunney Act responsibilities, has sought to achieve three principal objectives: (1) promotion of true and fair competition in the telecommunications long distance and equipment markets, (2) preservation of AT&T as a dynamic force, capable of research, manufacturing, and marketing in technologically advanced fields, and (3) protection of the principle of universal telephone service, accessible to all segments of the population regardless of income.

In its consideration of the decree, the Court was able to advance all of these objectives—in part by approving

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[284] The 471-page plan is a blueprint for the largest corporate reorganization in United States history. The decree itself describes the reorganization process only in the most general terms.

[285] Many of the submissions of the parties and the intervenors (*e.g.*, states, AT&T's competitors, consumer groups) were detailed and voluminous. For example, one intervenor—MCI—filed a total of over 850 pages of memoranda, exhibits, and other documents, and AT&T's March 1983 Response alone was 617 pages in length. For the first time in the Bell System reorganization process, the Operating Companies participated in the judicial proceedings in their own right. A hearing was held on June 2, 1983, at which the parties, several intervenors, and the chief executives of the Regional Companies gave their views on several particularly controversial issues. See notes 3 and 4 *supra*.

[286] The Court's powers under the Tunney Act are, of course, limited (see 552 F. Supp. at 151) and in passing upon the plan of reorganization, the Court likewise does not write on a clean slate but must conform to the provisions and principles of the decree itself.

various provisions of the proposal submitted by the parties over vigorous objection from others, and in part by requiring the substantial modification of a number of other provisions.[287] When it considered the plan of reorganization, the Court again had all three objectives in mind. However, it became apparent in the course of that consideration that the bulk of the actions which the Court had to take to achieve consistency of the plan with the decree tended primarily to promote the vitality of the Operating Companies[288] and the principle of universal service.[289]

[287] Among the actions which tended to further the cause of competition were the approval of the divestiture from AT&T of the twenty-two "bottleneck" local companies, the prohibition on the entry of these companies into business ventures where their monopoly status might have given them an improper advantage, and the requirement that these companies must provide equal access to all of AT&T's interexchange competitors. The Court also prohibited AT&T for a period of seven years from entering the electronic publishing market.

Actions designed to preserve AT&T's effectiveness included the rejection of proposals which would have required that company to divest itself of Western Electric and Bell Laboratories, prohibited it from utilizing sophisticated "bypass" technologies, and otherwise limited the scope of its operations. The Court also approved the removal of the restrictions imposed upon AT&T by the 1956 consent decree.

The vitality of the Operating Companies and the goal of universal telephone service were promoted, *inter alia*, by modifications which permitted the entry of the local companies into the printed advertising directory market and customer premises equipment market.

[288] These actions will, of course, to some degree affect existing and potential competitors of AT&T, suppliers of products, and others within and without the telecommunications industry. But in passing upon the plan of reorganization, the Court was principally called upon to decide "internal" matters between AT&T and the Operating Companies, and for that reason it is not particularly surprising that the primary impact of the decision is on the local companies and their financial well-being.

[289] This is not to say that other objectives were not advanced. Thus, the Court approved much of the AT&T plan, and it rejected proposals which would have improperly saddled AT&T with substantial costs, *e.g.*, the direct costs of providing equal access and reconfiguring the

These actions, which are described in detail in the body of the Opinion, include the assignment of the "Bell" name and logo to the Operating Companies (Part III(C) of the Opinion); imposition of the requirement that the Operating Companies be granted licenses to all patents acquired by the Bell System (Part IV(A)), along with appropriate sublicensing rights (Part IV(B)); the grant of authority to the Operating Companies to perform their own Official Services functions rather than to have to lease the necessary facilities from AT&T or other interexchange carriers (Part VI(A)); approval of the establishment of a Central Staff Organization which will give effective logistical support to the Operating Companies (Part VIII); imposition of the requirement that AT&T stand as the ultimate guarantor of the costs of equal access and network reconfiguration (Part I); and the approval of local access and transport areas (LATAs) which avoid substantial, costly network rearrangements (Part VII(A)).

The fundamental purpose of the decree under the antitrust laws is to create conditions which will reduce the cost of telecommunications service to the public—individual consumers, business, and govern-

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network (Part I(C) of this Opinion) and the sole financial responsibility for the Bell System's contingent antitrust liabilities (Part II). In order further to promote competition in telecommunications services, the Court, *inter alia*, rejected joint use by AT&T and the Operating Companies of the name "Bell" (Part III(A)), required the access the Operating Companies provide to AT&T's competitors to be of sufficiently high quality so that voice and data customers will be unable to detect any difference (Part I(A)), and required the provision of equal access in the intra-LATA field and the densely populated "corridors" in the New York-New Jersey-Philadelphia areas (Part VII(B)). In the interest of protecting the rights of AT&T employees, the Court made explicit that with respect to various subjects (*e.g.*, pension benefits) the decree does not relieve AT&T of its obligation to bargain collectively. (Part V(A)).

ment.[290] Competition in the long distance and telephone equipment markets is already bearing fruit in the form of lower prices and wider choices.[291] In the view of this Court, it is not necessary that these favorable developments be accompanied by the imposition of higher rates for local service.

One of the Court's principal aims throughout the public interest process has been to ensure that divestiture would not bring about or contribute to local telephone rate increases. While the parties to this proceeding have acknowledged that this effort was successful and that neither the decree nor the divestiture has caused or will cause local rates to rise,[292] these rates will nevertheless be going up, albeit for reasons unrelated to the reorganization of the Bell System.

As the Court has previously noted, and as it elaborates at pp. 259-61 *supra*, decisions taken by federal regulators regarding access charges will have the effect of increasing the cost of local service to residential subscribers.

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[290] Cost reductions need not, and in the Court's view will not, be achieved at the expense of quality and reliability. See Part VIII of the Opinion where the Court approved the setting of uniform standards so as to maintain the quality of the telephone network.

[291] A number of interexchange carriers and telephone equipment manufacturers and dealers have entered these fields or have vastly expanded their operations. The result has been that the prices of long distance service and customer premises equipment are falling and that telephone and related apparatus are becoming available in unprecedented varieties. These trends may be expected to continue and, indeed, to accelerate.

[292] See, *e.g.*, Department of Justice Supplemental Memorandum, June 10, 1983, at 8 (decree will not, and has not, caused adverse effects on local rates); AT&T Response of May 5, 1983, at 10-21 (local rates are going up but not because of divestiture); see also, Response of the Federal Communications Commission, June 13, 1983, at 4 n.5 (FCC decision not a product of divestiture since Commission had proposed customer access charges well before Court accepted decree).

The Court has no authority to countermand those decisions.[293] It does, however, have the authority to take them into account—not conclusively, certainly, but as support for determinations which are indicated in any event. That is what it has done here. The modifications it is requiring to be made in the proposed plan of reorganization should assist in moderating the pressure for local rate increases, whatever their source.[294]

The telecommunications industry as a whole has a bright future for, as the Court previously observed,[295] we live in an age in which information and its transmission are central to the commonweal and a flourishing economy. No one can predict which company or group of companies will be able best to take advantage of the opportunities which lie ahead. To a large extent this will depend upon their own efforts and performance,[296] and to a lesser degree upon the wisdom of those who will exercise regulatory authority over various segments of the industry at the federal and local levels. As indicated above (Part IX), the Court's own oversight over the Bell System divestiture process will end with the approval of the plan of reorganization.[297]

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[293] See 47 U.S.C. §402.

[294] Requests for rate increases by local telephone companies are apparently sought to be justified in some instances by references to the divestiture. Such reliance is unjustified. See note 292 *supra*.

[295] 552 F. Supp. at 164-65.

[296] See, *e.g.*, Fortune, *Breaking Up The Phone Company*, June 27, 1983.

[297] The Court assumed control of this case in the summer of 1978. Pretrial proceedings were designed and announced in September of that year (461 F. Supp. 1314), and they took a little over two years to complete. Trial began in January 1981, and it was within weeks of completion when, in January 1982, the parties settled the case by the consent decree referred to above.

AT&T (including Western Electric and Bell Laboratories) as well as the Operating Companies appear to be led by talented managers, scientists, and engineers; moreover, these entities will continue to command immense personal and material resources. There is no reason to believe that the separate parts of the reorganized Bell System will not prosper in the new environment or that they will fail to contribute significantly to the American economy.

B. Actions on the Motions

Motions of AT&T and of the Department of Justice seeking approval of the plan of reorganization are pending.[298] These motions will favorably be acted upon after the Court is advised that the following modifications[299] are agreed to by the parties:[300]

1. If by January 1, 1994, the Operating Companies in the aggregate have not recovered the costs of providing equal access and network reconfiguration (as defined in AT&T's Consolidated Application filed with the Federal Communications Commission on March 1, 1983), plus financing expenses, through their collection of access charges from the interexchange carriers, AT&T will reimburse the Operating Companies in the amount of any re-

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[298] Issues relating to the LATAs are not a part of the plan of reorganization as such. However, the Court expects compliance with the decisions made with respect to such issues in the Opinion of April 20, 1983, and the present Opinion. It also expects the parties to comply with the other directions contained in these two documents.

[299] All such modifications will supersede the existing provisions of the plan of reorganization to the extent of any inconsistency.

[300] Section VIII(J) of the decree provides that the plan of reorganization "shall not be implemented until approved by the Court as being consistent with the provisions and principles of the decree." The Court considers that the plan will not be consistent with the decree until modified as required herein.

maining deficit. For purposes of this provision, "costs" shall mean the actual costs incurred by the Operating Companies, as distinguished from the estimates in the Consolidated Application. A preliminary accounting will be provided to the Court at the close of the Operating Companies' equal access and network reconfiguration program or by January 1, 1989, whichever is earlier, and a final accounting not later than January 1, 1994.

2. Beginning on the date of divestiture, AT&T will cease to use the word "Bell" in its corporate name and in the names of its subsidiaries or affiliates, other than Bell Laboratories and AT&T's foreign subsidiaries or affiliates; and beginning on the same date, AT&T will cease to use the "Bell" name and the Bell trademarks, or either, on any equipment sold by it in the United States after that date, except for equipment manufactured or purchased by AT&T prior to that date. In the event that substantial efforts have been made by AT&T by November 1, 1983, to acquaint the public with a new name to replace the name "American Bell," and for good cause shown, the Court will extend the use of that name by AT&T for an additional six months following divestiture in connection with the sale, but not the manufacture or purchase, of equipment.

The divested Operating Companies, the Regional Companies, or either, may use the "Bell" name and the Bell trademarks in connection with the services they perform and on equipment they use or sell, and they may use the word "Bell" in their corporate names, provided that the "Bell" name is modified so as to identify the particular company, and provided further that on equipment sold any Bell trademark is accompanied by the corporate name of the respective Operating Company or Regional Company.

3. AT&T will grant to each Operating Company nonexclusive and personal royalty-free licenses to use telecommunications equipment and operational methods covered by all existing patents owned or controlled by AT&T and all other patents issued to AT&T on or before years after the date of divestiture.

AT&T will grant to each Operating Company the right to sublicense all AT&T patents to manufacturers for use only in providing the Operating Companies with goods and services embodying the inventions of the patents.

4. In determining whether the use made by an Operating Company of facilities or other assets predominates over that made by AT&T within the meaning of section VIII(G) of the decree, the capacity of a facility or other asset devoted to Operating Company Official Service functions will be included as part of the Operating Company's use. Nothing in the decree precludes an Operating Company from constructing or maintaining facilities or other assets devoted to Operating Company Official Service functions.

5. The Operating Companies will not provide inter-LATA order writing, order typing, or other provisioning exclusively for AT&T.

6. The decree does not relieve AT&T and the Operating Companies from bargaining in good faith with any labor union, except with respect to the division of the Bell System Pension Plan into nine separate plans; the actuarial methodology specified in the plan of reorganization; and the elimination, one year following the date of divestiture of unlimited portability of service credit.

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Harold H. Greene
United States District Judge

Dated: July 8, 1983

MEMORANDUM

(Filed July 28, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

MEMORANDUM

I

**AT&T has asked for partial reconsideration of the Court's ruling of July 8, 1983, requesting that the Court delete Modification 1[1] which requires that AT&T**

[1] This Modification reads as follows:

If by January 1, 1994, the Operating Companies in the aggregate have not recovered the costs of providing equal access and network reconfiguration (as defined in AT&T's Consolidated Application filed with the Federal Communications Commission

guarantee the costs of providing equal access and of reconfiguring the network to conform to the LATAs (hereinafter generally referred to collectively as access costs or access expenses). The principal contention supporting the request for an outright elimination of the guarantee provision[2] is that this provision would improperly add to AT&T's obligation under the decree.[3]

As the Court previously pointed out (Opinion of July 8, 1983 at 206-11), there are two bases under the decree for requiring AT&T to bear at least part of the cost of access, whether in the form of a guarantee or otherwise. First, although section I(A)(1) requires AT&T to transfer to the Operating Companies adequate facilities to enable the local companies to meet the equal access requirements, the transfers of equipment provided for under the plan of reorganization will clearly not be sufficient to achieve that purpose. Second, AT&T consistently represented to the Court that, even though the company would not pay the access expenses directly, it

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on March 1, 1983), plus financing expenses, through their collection of access charges from the interexchange carriers, AT&T will reimburse the Operating Companies in the amount of any remaining deficit. For purposes of this provision, 'costs' shall mean the actual costs incurred by the Operating Companies, as distinguished from the estimates in the Consolidated Application. A preliminary accounting will be provided to the Court at the close of the Operating Companies' equal access and network reconfiguration program or by January 1, 1989, whichever is earlier, and a final accounting not later than January 1, 1994.

[2] Other points made by AT&T essentially relate to the request for a proviso to the Modification and are considered under II *infra*.

[3] AT&T also claims that the issue was not briefed or otherwise considered prior to the Court's decision on July 8, 1983, but this claim is difficult to understand. Dozens of memoranda with supporting materials were submitted to the Court on the question whether the access costs should more appropriately fall on AT&T or on the Operating Companies, and this was also one of the subjects on which argument and testimony were adduced at the June 2, 1983 hearing.

The choice thus rests with the various regulatory bodies.[17] They may either so adjust the depreciation schedules for equipment used to provide equal access or network reconfiguration as to accommodate the requirements of Modification 1, or they may decline to do so, recognizing that if they elect this course not all the costs may be recovered within a ten-year period and AT&T will be relieved of its obligation to that extent to make up the difference.

The Court denies AT&T's motion for partial reconsideration insofar as it requests that the Court strike Modification 1, but it grants that motion insofar as it requests the addition to the Modification of a proviso.[18] Accordingly, Modification 1 is hereby amended by the addition of the following language:

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[17] This solution also appropriately meets concerns expressed by the Federal Communications Commission (Comments at 2) and by NARUC (Response at 5) that the Court's decision might improperly interfere with the authority of the regulators.

[18] Several of the intervenors propose various measures in other areas of the plan of reorganization in order to counterbalance what they regard as the effects of the proviso. Thus, California proposes (Opposition at 9-10) that the Court assign the so-called "Account 232" to AT&T, and MCI suggests (Opposition at 3) that the Court's modification with respect to patent licensing will have a beneficial impact on the recovery of the access costs. The plan of reorganization, as it was required to be modified in the July 8, 1983 Opinion, is carefully balanced to achieve the decree's purposes and objectives. The proviso is not sufficiently significant to call that balance into question and thus to provoke reconsideration of other aspects of the plan.

California also suggests (Opposition at 5-6) that

> [t]hroughout the nation, BOCs are presenting regulatory authorities with rate increase proposals requesting not only substantial increases in total revenue but also drastically restructured rate designs, featuring 100 to 300 percent increases in basic monthly rates . . ., occasional reductions in toll rates [and] substantial customer access line charges . . . .

To the extent that these requests are claimed to be based on the divestiture as presently structured, they have no justification.

would do so indirectly through the carrier access charges.[4] It now appears, however, that for several reasons discussed in the July 8, 1983 Opinion, the carrier access charges may not be adequate to reimburse the Operating Companies for these costs. Hence the guarantee required as a prerequisite to the Court's approval of the plan of reorganization.

The argument made by AT&T, and supported by the Department of Justice, that the guarantee would impose an obligation on the company that would be inconsistent with what the parties call the decree's "basic premise"—that the access costs be recovered through access charges paid by all interexchange carriers, not merely AT&T[5]—thus misses the point, for it fails to consider those features which embody a special AT&T obligation not shared by other carriers: the provisions of section I(A)(1) and the representations made to the Court by AT&T.[6]

All of these subjects were fully explored by the parties and considered by the Court prior to the issuance of the

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[4] While all interexchange carriers will pay such access charges, AT&T, as the largest carrier, will contribute the lion's share.

[5] AT&T Memorandum at 3-4; Department of Justice Response at 2.

[6] Moreover, as the National Association of Regulatory Utility Commissioners (NARUC) points out,

> [i]t would be fundamentally unfair if AT&T, whose interstate toll operations were sheltered by the refusal to provide equal access, should be allowed to unload the massive costs of complying with the decree upon the BOCs.

Response at 2. On this basis, the Court also rejects AT&T's demand that it strike the reference in the July 8, 1983, Opinion to AT&T's prior obligation to provide equal or substantially equal access. Motion at 6-7 note*. If this issue should arise in other, private litigation, the tribunals having jurisdiction will, of course, draw their own conclusions based on their understanding of court and FCC precedents.

July 8, 1983 Opinion: AT&T's motion adds nothing new on any of the underlying issues; and the Court will therefore deny that motion to the extent that it requests the deletion of Modification 1.

II

The essence of AT&T's argument in support of the attachment of a proviso to the Modification lies in the claim that the Operating Companies and the local regulators would have and might exercise the opportunity to establish access charges that would be insufficient for full cost recovery. The result of such actions would be that the costs would ultimately be recovered from AT&T pursuant to the guarantee. This, according to AT&T, is not the purpose for which the Modification was designed. That understanding is correct.

The Operating Companies, assured under the guarantee provision of reimbursement from AT&T at the end of the ten-year period specified in the Modification, would have a significant incentive consistently to underrecover access costs prior to that time;[7] the regulators would have a similar incentive to deny full recovery of such costs;[8] and AT&T's competitors would have an incentive to encourage these trends.[9] In the judgment of the Court it is quite likely that, absent some countervailing mechanism, these entities will act on these incentives.

[7] This would lower rates and thus stimulate usage, and it would also tend to divert the equal access obligation from the local companies to AT&T.

[8] The resulting lower intra-LATA toll rates would obviously be popular with the public the regulators serve.

[9] To the extent that AT&T, as a result of the guarantee, ultimately paid for the costs of providing equal access, its competitors would be relieved of the obligation of paying for that access through interexchange access charges.

The Court was not unmindful of this contingency when it issued the July 8, 1983 Opinion. Indeed, it was for that reason that it required AT&T and the Operating Companies to file prior to divestiture a description of the accounting methods which would be used for identifying the access costs and for determining whether and when they had been recovered. Opinion at 210 note 37. The Court had in mind that, if AT&T and the Operating Companies agreed on the procedure and substance with respect to such recovery, there would be no need for further judicial intervention; if these parties did not agree (essentially because of a dispute similar to that generated by AT&T's present motion) the Court could take steps before divestiture to guard against the contingencies feared by AT&T. By its motion AT&T has brought the issue to a head now, and there is no reason for delaying consideration of this subject.

The July 8, 1983 ruling represents the Court's determination that the somewhat conflicting requirements of the decree[10] can best be harmonized by requiring the Operating Companies to incur the access expenses while requiring AT&T to provide the guarantee embodied in Modification 1. Implicit in that Modification is the principle that AT&T shall guarantee all access costs legitimately incurred and legitimately unrecovered. Equally implicit is the corollary: that AT&T need not provide a guarantee with respect to costs which remain unrecovered as a consequence of actions by Operating Companies or regulators designed improperly to divert such costs to AT&T. The proviso proposed by AT&T would make the latter objective explicit,[11] and it would

[10] Compare, *e.g.*, section I(A)(1) with Appendix B.

[11] Essentially, the protection of AT&T is accomplished in the proviso by the clauses relieving AT&T of its obligation if the Operating Companies fail to file access charge tariffs designed to recover all costs included within the guarantee, or if the regulators refuse to allow such tariffs to take effect.

do so—as will now be seen—without in any way weakening the guarantee itself.

Several of the intervenors[12] argue that the proviso would have the practical effect of nullifying the guarantee obligations. The theory underlying these arguments is that, if due to market forces or substantial bypass by AT&T, there is a shortfall in any one year in the recovery of carrier access charges to pay for the access costs, the Operating Companies will under the proviso be compelled to file, and the regulators will be compelled to approve, a higher tariff the following year, and so on every year until the end of the guarantee period. This process, it is said, would automatically and inevitably relieve AT&T of all obligations on the following basis. If the tariffs were designed so as to recover all necessary costs, there would never be a shortfall; on the other hand, if the tariffs were not designed to recover all necessary costs, they would violate the proviso and AT&T would be discharged of its obligation on that basis.

That analysis misconceives the breadth of the guarantee and the relatively narrow focus of the proviso. As AT&T has pointed out (Reply at 8-9):

> The obligation would still require AT&T to stand as the ultimate guarantor of whatever equal access and network reconfiguration costs are allowed in the BOCs' tariffs in the ten years following divestiture. If market conditions ultimately prevent the BOCs from recovering those costs by January 1, 1994—despite their inclusion in tariffs intended to produce full recovery—AT&T pays the balance, even as the guarantee would be conditioned by the proviso.

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[12] *E.g.*, Maine, p. 2; NARUC, pp. 4-7; GTE, p. 7; SBS, p. 2.

Properly construed, then, the effect of the Modification in combination with the proviso will be to protect AT&T from manipulation by the Operating Companies or the regulators; at the same time, these provisions will not excuse AT&T from the guarantee obligation in the event that there is a shortfall in the recovery of carrier access charges for access cost purposes as a result of market forces or bypass by AT&T.[13] Under the decree and in equity, that is as it should be.[14]

Questions have been raised by some (*e.g.*, SBS Memorandum at 3) regarding the duration of the

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[13] In the event that at the conclusion of the guarantee period, there is a dispute as to the cause of any shortfall, the Court will resolve that dispute as provided for on pp. 210-11 of the Opinion of July 8, 1983.

[14] The proviso proposed by AT&T includes a footnote which reads as follows:

> To the extent that network reconfiguration costs relate to the BOCs' provision of other services (such as intraLATA toll), rather than to carrier access services, the BOCs will be required to include such costs in tariffs for those other services which are filed and allowed to become effective in accordance with this proviso, and any amounts thus recovered shall count toward reimbursement of the BOCs' costs of network reconfiguration.

Network facilities to be constructed will, of course, be used in part for services other than interexchange access (*e.g.*, for intra-LATA access or intra-LATA toll services), and accordingly a portion of the investment in these facilities will normally be recovered from services other than such access. On this basis, it is appropriate, therefore, that any funds received by the Operating Companies from these other sources be counted toward AT&T's reimbursement obligation. It was for this reason that the Court required in its July 8, 1983 Opinion that the Operating Companies keep records to isolate access expenses from expenses they would have incurred in any event (Opinion at 210 note 37), and it is on the same basis that it approves the inclusion of this footnote.

It should be noted that this provision will not compel regulators to determine that any portion of network reconfiguration costs relates to services other than carrier access services; it simply provides that *if* the regulators make such determinations, AT&T will be protected from having to pay under the guarantee even though, in reality, there was no deficit.

guarantee period. Modification 1 envisages the recovery by the Operating Companies of the costs of access within ten years. AT&T and others (*e.g.*, the Department of Justice) have pointed out that under current regulatory directives, many major capital investments must be depreciated over extended periods of time, some in twenty-five years. The Court is thus presented with the choice of either substantially extending the guarantee period or retaining the ten-year period notwithstanding the various existing or proposed depreciation schedules.

After giving the subject careful consideration, the Court has decided to retain the ten-year deadline.[15] Any change in that regard would create unnecessary and inappropriate entanglements between AT&T and the Operating Companies well into the next century.[16] Moreover, depreciation schedules vary, depending not only upon the equipment involved but also upon the practices of the several state and federal regulators, and it would be difficult, if not impossible, to tailor the guarantee to meet all these contingencies. Finally, the various depreciation schedules are not immutably fixed in the law but are subject to change by the regulators.

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[15] The Court recognizes that one consideration cuts the other way: a ten-year schedule, as California points out (Opposition at 7), may inflate the Operating Companies' annual access costs in the near term. However, that increase in costs must be kept in perspective. Even if $3 billion will have to be recovered in the ten-year period, the total amount would still only be two percent of the over $150 billion that is estimated to be collected by the Operating Companies in access charges. See Department of Justice Response, Attachment B at 6. Thus, the effect on rates of a ten-year recovery period vs. some longer period would not be substantial, and even that effect could further be mitigated by the regulators.

[16] For the same reason, the Court rejects the suggestion of the United Church of Christ (Opposition at 8) that AT&T be relieved of the guarantee only to the extent that the Operating Companies may be able to recover costs after 1994.

Provided, however, that with respect to any Operating Company, AT&T's obligation shall be discharged to the extent that: (a) the Operating Company fails annually to file carrier access tariffs designed to recoup any then-unrecovered equal access and network reconfiguration* costs by January 1, 1994; or (b) any regulatory commission refuses to permit such tariffs to take effect; or (c) regulatory requirements for the depreciation or amortization of equal access and network configuration investment cause any portion of the investment not to be recognized as a cost of ratemaking in periods prior to January 1, 1994.

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* To the extent that network reconfiguration costs relate to the BOCs' provision of other services (such as intraLATA toll), rather than to carrier access services, the BOCs will be required to include such costs in tariffs for those other services which are filed and allowed to become effective in accordance with this proviso, and any amounts thus recovered shall count toward reimbursement of the BOCs' costs of network reconfiguration.

It is the Modification as so amended which AT&T and the Department of Justice will be required to incorporate in the plan of reorganization as a prerequisite to the Court's final consideration and approval of that plan.

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Harold H. Greene
United States District Judge

Dated: July 28, 1983

MEMORANDUM

(Filed: August 5, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

MEMORANDUM

Several motions for reconsideration or clarification of the Court's July 8, 1983 Opinion have been filed. This Memorandum disposes of all such motions.[1]

[1] To the extent that motions or individual arguments made in motions are not addressed herein, they either raise issues which were previously fully considered or are deemed to lack merit for other reasons. However, the Operating Companies' proposed provision of cellular radio services across LATA boundaries, which is not part of the plan of reorganization but constitutes a request for an exception under Section VIII(C) of the decree, will be considered at a later time.

1. MCI Communications Corporation has moved for clarification of Modification 3, which modifies the provisions of the plan of reorganization with respect to patents. MCI argues that computer software is subject to this modification, and that AT&T must grant to the Operating Companies royalty-free licenses thereto as well as the right to sublicense where the provision of goods and services to these companies is involved.

The Court stated in its July 8, 1983 Opinion that, for purposes of the plan of reorganization, "patents" includes non-patented technical information. Opinion at 216 note 100. However, as the Court indicated in the very next sentence of that footnote, it was referring in the technical information context to such information as was funded by the license contract between AT&T and the Operating Companies. Computer software has not been so funded.

More broadly, as the discussion in Part IV of the July 8, 1983 Opinion demonstrates, insofar as technical information (as distinguished from patents) is concerned, the Court was concerned in Modification 3 with the issues raised in the "Patents" section of the plan of reorganization, in particular note 399 at p. 411 of the plan. That footnote flatly states that "[t]he BOCs will not be granted any licenses relating to patents or any other technical information that relate solely to provision of CPE, interLATA service or any BOC services now prohibited by the Decree." The July 8 Opinion made it clear that this restriction was unacceptable under the purposes and principles of the decree and the representations that had been made to the Court. This, in turn, led to the requirement of Modification 3.

Other portions of the plan of reorganization deal with non-patented technical information in completely different contexts. For example, Part II(A)(1) (pp. 341-369

of the plan) discusses in considerable detail the assignment of various types of computer software. It was not the Court's intention to disapprove these portions of the plan *sub silentio.*[2] Indeed, the two reasons given in the July 8 Opinion for granting to the Operating Companies more extensive patent rights than originally provided for by the plan of reorganization—(1) recognition of past contributions to research they had made through the licensing contracts, and (2) the reasonableness of the removal of the mandatory patent licensing provisions of the 1956 decree[3]—are not applicable to the type of non-patented, computer software which is the subject of MCI's motion.[4] These parts of the plan were not affected by Modification 3, and they remain in effect.

To the extent that clarification is required to resolve any seeming inconsistency between the Court's reference to technical information in note 100, on the one hand, and its implicit approval of the plan's treatment of non-patented technical information which AT&T did propose to share with the Operating Companies, on the other,[5] it is hereby resolved as described above. MCI's motion will accordingly be denied.

2. Several intervenors ask the Court to reconsider its approval of the assignment of the so-called Account 232

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[2] The provisions in the plan regarding computer software represent complex arrangements some of which were substantially modified by AT&T following Department of Justice Objections. See, *e.g.*, Response of Department of Justice to Comments at 144-52.

[3] Opinion of July 8, 1983 at 245-47.

[4] See AT&T Response to Objections at 426-29.

[5] *I.e.*, technical information not related to CPE, inter-LATA service, or other Operating Company services prohibited by the decree.

to the Operating Companies and to assign the Account instead to AT&T.[6] That request will likewise be denied. In-place wiring, which is a principal item in Account 232, is as much a "bottle-neck" as are the subscriber access lines.[7] To assign such wiring to AT&T would be to insert AT&T-controlled facilities between the Operating Companies and the subscribers, and such an assignment would thus be entirely inconsistent with the basic purposes of the decree.[8]

Account 232 also includes the capitalized labor costs associated with the installation and testing of customer premises equipment, and a theoretical case could be made that, since under the plan embedded CPE is being assigned to AT&T, so should be this portion of Account 232. However, the Court was and is persuaded by AT&T's argument, for the reasons stated in AT&T's Response to Objections at 154-55, that there is no practical way to separate out the various handling costs.[9] The provision made in the plan of reorganization regarding Account 232 is consistent with the decree and otherwise reasonable, and there is no basis for reconsidering the Court's approval of the plan in this regard.

3. GTE Corporation has petitioned the Court for limited reconsideration of that part of the Court's July 8, 1983 Opinion which approved the Operating Companies' classifications (as either intra-LATA or inter-LATA) of

[6] The Court did not discuss this issue in the July 8, 1983, Opinion, but it was considered. Opinion at 196 note 2, and at 3.

[7] Much inside wiring is wire that is embedded in conduits, and it is not replaceable by, nor often even accessible to, the customer.

[8] See *Litton Systems, Inc.* v. *Am. Tel. & Tel.*, 700 F.2d 785 (2d Cir. 1983).

[9] See also, the FCC's treatment of this issue, *Amendment of Part 31 (Uniform System of Accounts)*, CC Docket No. 79-105, 85 F.C.C.2d 818, 823-30 (1981).

traffic between their territories and Independent telephone company territories. Opinion of July 8, 1983 at 301-08. The basis for this request for the reconsideration of nineteen out of hundreds of such classifications is that new information regarding homing and network arrangements was revealed for the first time during the development of the exchange areas under the proposed consent decree in *United States* v. *GTE Corp.*, Civil Action No. 83-1298, (filed May 4, 1983), which is pending before this Court. See GTE Petition at 2.

Of the nineteen classifications at issue, in eleven instances the relevant Operating Company does not oppose GTE's reclassification proposal.[10] These proposals are reasonable and consistent with the decree, and they will accordingly be deemed incorporated in the plan of reorganization.

Of the remaining eight GTE proposals, in two instances the Operating Company does not oppose a temporary reclassification pending the completion of certain modernization programs (which was the basis for the Operating Company's original proposal).[11] Such a temporary reclassification makes sense in view of current network arrangements, and the Court will approve it for these two areas on such a basis. In another case, permis-

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[10] These proposals relate to the following areas: Indiana-Lafayette; Oklahoma-Guymon; South Carolina-Florence; Illinois-Olney; Illinois-Macomb; Pennsylvania-Erie; Texas-Texarkana; Kentucky-Winchester; Michigan; Oregon; and Washington. With respect to the last three areas, the respective Operating Company has indicated that the classifications in these states are already being revised as required by the Court's July 8, 1983 Opinion, and that they will therefore be consistent with the GTE proposals. Response of the Operating Companies to GTE Petition at 6-7.

[11] The proposals in this category relate to the areas of Illinois-Bloomington and Illinois-Kewanee. Response of the Operating Companies to GTE Petition at 4, 7.

sion is hereby granted for the reclassification which GTE proposes, upon completion of the rehoming project.[12]

In two instances, the Operating Company and GTE are in agreement, but the Department of Justice has correctly pointed out that the Operating Company should be permitted, but not required, to service the adjacent area.[13] With respect to the three remaining proposals, relevant Operating Company opposes the reclassification—at least at this time—and GTE has not demonstrated that the classification as originally proposed by that Operating Company, and approved by the Department of Justice and the Court, is unreasonable or inconsistent with the decree.[14] Accordingly, that part of GTE's motion which relates to these five areas is denied.

4. The Public Service Commission of Kentucky has moved for reconsideration of the Court's decision to deny consolidation of the Winchester and Louisville LATAs. The Commission argues that the incremental loss of intrastate toll revenue that will be occasioned by three LATAs rather than two will require increases in local rates. However, the Commission has failed to note that access charges to be collected from the interexchange carriers can, if set properly, make up for any loss

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[12] This will enable the association of the Chesapeake exchange with the Columbus LATA when the exchange is rehomed in 1984.

[13] These two proposals relate to Indiana-Terre-Haute and West Virginia-Bluefield.

[14] These proposals relate to the following areas: Illinois-Chicago; Ohio-Medina; and California-Oxnard. With respect to the last of these areas, Pacific Telephone has indicated that it is presently discussing the resolution of this matter with the Department of Justice. Response of the Operating Companies to GTE Petition at 3. As the Court indicated in the Opinion of July 8, 1983, the Bell Operating Companies may, under the decree, subsequently petition the Court for reclassification or for exceptions in regard to service between their own areas and Independent territory. Opinion of July 8, 1983 at 305 n.238.

of revenue to South Central Bell. In any event, significant competitive advantages would flow from three LATAs. The Department of Justice has previously argued in favor of three LATAs on this basis; and the Public Service Commission has not demonstrated that the Court ought to disturb its prior decision that three LATAs are appropriate in Kentucky.[15] The motion is denied.

5. New York Telephone Company has expressed concern that the July 8, 1983 Opinion may have placed territorial restrictions on the Operating Companies' provision of directory advertising services. That concern is unwarranted. As the company correctly surmised, when the Court made mention of activities outside an Operating Company's territory,[16] it was referring to the Bell logo standing alone and the Bell name without a modifier. The decree and the plan do not limit the provision of directory advertising or of customer premises equipment to prescribed geographical territories.

6. The American Council of the Blind, the Paralyzed Veterans of America, and others are concerned about the transfer to AT&T of embedded specialized equipment for the disabled, such as teletypewriters and large button telephones, the price of which may conceivably no longer be subsidized after the transfer. The Court's approval of the decree's provisions regarding embedded CPE is, of course, without prejudice to whatever equitable arrangements may be made among AT&T, the Operating Companies, and the representatives of the disabled regarding continued subsidization of such equipment. See also, The Telecommunications for the Disabled Act, P.L. 97-410 (1982).

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[15] South Central Bell is neutral on this issue.

[16] July 8, 1983 Opinion at 238-39.

ORDER

(Filed September 7, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

ORDER

On August 10, 1983, the People of the State of California and the Public Utilities Commission of the State of California noted an appeal from the order entered by this Court on August 5, 1983, approving AT&T's plan of reorganization as amended.[1] On August 25, 1983, the

[1] California's notice of appeal states that it is also appealing orders filed July 8, 1983 and July 28, 1983. The August 5, 1983 order approved AT&T's plan in accordance with the Court's Opinions filed on the earlier dates.

AT&T is to divest itself of the local operating companies on January 1, 1984.[7] This divestiture, apparently the largest corporate reorganization in history, will directly affect millions of employees and shareholders, the nation's telephone subscribers, AT&T's competitors, the telecommunications industry in general, and the responsibilities of federal and state regulatory bodies. On the basis of the January 1 deadline, the various public and private bodies are currently implementing detailed[8] plans to effectuate the reorganization. Uncertainty regarding the legal status of that reorganization would have serious adverse consequences to the various private interests involved as well as to the public interest. The consequences would be multiplied if the divestiture proceeded on January 1, 1984, while the plan of reorganization was still under challenge in the courts.

Factors similar to these played an important part in this Court's November 10, 1982, certification. Now, that the divestiture date is less than four months rather than almost fourteen months away, a speedy, final resolution of the legal situation is all the more necessary. It is unlikely that such a resolution could be secured through the normal process of review by the U.S. Court of Appeals to be followed by a petition for writ of certiorari to the Supreme Court.

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[7] Under the judgment, this reorganization must take place not later than February 24, 1984.

[8] This includes such matters as the distribution of the assets of the Bell system, assignment of the employees, the establishment of seven new local holding companies and a central staff organization, and treatment of the shares of stock.

For these reasons, the Court certifies this 7th day of September, 1983, that immediate consideration by the Supreme Court of the appeal and of any additional appeals filed hereafter[9] is of general public importance in the administration of justice.

This order and the accompanying papers[10] shall forthwith be filed in this Court and transmitted to the Clerk of the Supreme Court, with copies to the Clerk of the U.S. Court of Appeals.

Harold H. Greene
United States District Judge

[9] See *United States* v. *AT&T*, No. 82-2286 (D.C. Cir. Slip Opinion August 12, 1983).

[10] Attached to this order are the order of August 5, 1983, and the opinions dated July 8, 1983 and July 28, 1983.

NOTICE OF APPEAL

(Filed September 13, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INC.; AND BELL TELEPHONE LABORATORIES, INC.,<br>Defendants. | Civil Action No. 74-1698 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

*15 U.S.C. § 16:*

(a) A final judgment or decree heretofore or hereafter rendered in any civil or criminal proceeding brought by or on behalf of the United States under the antitrust laws to the effect that a defendant has violated said laws shall be prima facie evidence against such defendant in any action or proceeding brought by any other party against such defendant under said laws as to all matters respecting which said judgment or decree would be an estoppel as between the parties thereto: *Provided*, That this section shall not apply to consent judgments or decrees entered before any testimony has been taken. Nothing contained in this section shall be construed to impose any limitation on the application of collateral estoppel, except that, in any action or proceeding brought under the antitrust laws, collateral estoppel effect shall not be given to any finding made by the Federal Trade Commission under the antitrust laws or under section 45 of this title which could give rise to a claim for relief under the antitrust laws.

(b) Any proposal for a consent judgment submitted by the United States for entry in any civil proceeding brought by or on behalf of the United States under the antitrust laws shall be filed with the district court before which such proceeding is pending and published by the United States in

7. The Communications Workers of America yesterday for the first time requested that the Court clarify or reconsider language in the July 8, 1983 Opinion which may prohibit portability of pension benefits not only between AT&T and the divested entities but also among the Regional Companies and between them and the Central Staff Organization. See Opinion at 266. In view of the fact that AT&T and the Union are apparently at the present time engaged in collective bargaining, the Court inquired of AT&T whether it was prepared, on an informal and expedited basis, to express its agreement with the Union's interpretation, but AT&T responded that it could not do so. Accordingly, the issue will be resolved on the basis of briefing in accordance with the usual procedure.

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Harold H. Greene
United States District Judge

Dated: August 5, 1983

ORDER

(Filed August 5, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

ORDER

Upon consideration of the motion filed by AT&T on April 7, 1983 to approve the Plan of Reorganization, the proposed plan of reorganization as amended, the testimony given, and the oppositions, affidavits, comments, responses, and briefs filed with respect thereto;

It appearing that AT&T on August 3, 1983, agreed to the modifications required by the Court on July 8, 1983,

as qualified on July 28, 1983, and it appearing that the Department of Justice has likewise given its assent to such modifications, it is this 5th day of August, 1983,

ORDERED That the motion be and it is hereby granted, and it is further

ORDERED That AT&T's proposed plan of reorganization, dated December 16, 1982, as amended March 14, 1983, March 25, 1983, April 7, 1983, and August 3, 1983, be and it is hereby approved as consistent with the provisions and principles of the decree entered on August 24, 1982.

Harold H. Greene
United States District Judge

Dated: August 5, 1983.

United States moved for an order certifying the appeal[2] directly to the Supreme Court pursuant to 15 U.S.C. §29(b) (Expediting Act). AT&T supports the government's motion,[3] and no intervenor has opposed it.

On November 10, 1982, this Court certified appeals from its August 24, 1982 judgment in this case pursuant to the Expediting Act, and the Supreme Court accepted the case under that Act.[4] The considerations which support those decisions are equally applicable here.

Under the Expediting Act, direct Supreme Court consideration is appropriate where the underlying antitrust judgment involves matters of great and general importance to the public interest because of their "impact on the economic welfare of this nation." See H. R. Rep. No. 1463, 93rd Cong., 2nd Sess. 14 1974).[5] Even though it is not likely that the appeals will present questions of legal significance,[6] they are clearly of general public importance.

---

[2] It may be that additional appeals will be taken by other intervenors within the sixty-day period allowed by law. However, under the Expediting Act, this Court is required to act on the certification motion within thirty days after notice of appeal is filed.

[3] See AT&T Response to Motion of the United States for Certification of Appeals to the Supreme Court, filed August 26, 1983.

[4] On February 28, 1983, the Court entered an order affirming the judgment. *Maryland* v. *United States*, 103 S. Ct. 1240 (1983).

[5] In this respect, the standard is unlike that which the Supreme Court has applied under its general review power where the importance of the legal questions presented is generally deemed paramount. See Stern and Grossman, *Supreme Court Practice* at 254-317 (5th ed.). Indeed, last year the Supreme Court accepted direct appeals from the judgment of this Court in this case (indicating public importance within the meaning of the Expediting Act) and then affirmed by summary order (suggesting lack of substantive merit).

[6] The basic issue decided by this Court on August 5, 1983, was that AT&T's plan of reorganization is consistent with the judgment previously entered in this case.

NOTICE OF APPEAL

(Filed August 10, 1983)

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

| | |
|---|---|
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INC.; AND BELL TELEPHONE LABORATORIES, INC.,<br>Defendants. | Civil Action No. 74-1698 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY,<br>Defendants. | Civil Action No. 82-0192 |
| UNITED STATES OF AMERICA,<br>Plaintiff,<br>v.<br>AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,<br>Defendants. | Misc. No. 82-0025 (PI) |

## NOTICE OF APPEAL

Notice is hereby given that the People of the State of California and the Public Utilities Commission of the State of California appeal to the United States Court of Appeals for the District of Columbia Circuit from the orders of the District Court, filed on July 8, 1983, July 28, 1983 and August 5, 1983, approving American Telephone & Telegraph Company's proposed plan of reorganization, dated December 16, 1982, as amended March 14, 1983, March 25, 1983, April 7, 1983 and August 3, 1983 as consistent with the provisions and principles of the decree entered on August 24, 1982 modifying the judgment in *United States v. Western Electric Company, Inc. et al.*, Civil Action No. 82-0192, and dismissing the action in *United States v. American Telephone and Telegraph Co., et al.*, Civil Action No. 74-1698.

DATED: August 9, 1983.

Respectfully submitted,

JANICE E. KERR
J. CALVIN SIMPSON
GRETCHIN DUMAS
5066 State Building
San Francisco, CA 94102
(415) 557-0470
Attorneys for the People of the State of California and the Public Utilities Commission of the State of California

## NOTICE OF APPEAL

Notice is hereby given that the New York Department of Public Service hereby appeals to the United States Court of Appeals for the District of Columbia Circuit from the orders of the District Court, filed on July 8, 1983, July 28, 1983 and August 5, 1983, approving American Telephone & Telegraph Company's proposed plan of reorganization, dated December 16, 1982, as amended March 14, 1983, March 25, 1983, April 7, 1983 and August 3, 1983 as consistent with the provisions and principles of the decree entered on August 24, 1982 modifying the judgment in *United States v. Western Electric Company, Inc. et al.*, Civil Action No. 82-0192, and dismissing the action in *United States v. American Telephone and Telegraph Co., et al.*, Civil Action No. 74-1698.

DATED: September, 1983.

Respectfully submitted,

/s/ DAVID E. BLABEY per/CS
/s/ LAWRENCE G. MALONE per/CS
/s/ TIMOTHY P. SHEEHAN per/CS
Three Empire State Plaza
Albany, New York
(518) 474-2510
Attorneys for the New York State
Department of Public Service

the Federal Register at least 60 days prior to the effective date of such judgment. Any written comments relating to such proposal and any responses by the United States thereto, shall also be filed with such district court and published by the United States in the Federal Register within such sixty-day period. Copies of such proposal and any other materials and documents which the United States considered determinative in formulating such proposal, shall also be made available to the public at the district court and in such other districts as the court may subsequently direct. Simultaneously with the filing of such proposal, unless otherwise instructed by the court, the United States shall file with the district court, publish in the Federal Register, and thereafter furnish to any person upon request, a competitive impact statement which shall recite —

(1) the nature and purpose of the proceeding;

(2) a description of the practices or events giving rise to the alleged violation of the antitrust laws;

(3) an explanation of the proposal for a consent judgment, including an explanation of any unusual circumstances giving rise to such proposal or any provision contained therein, relief to be obtained thereby, and the anticipated effects on competition of such relief;

(4) the remedies available to potential private plantiffs damaged by the alleged violation in the event that such proposal for the consent judgment is entered in such proceeding;

(5) a description of the procedures available for modification of such proposal; and

(6) a description and evaluation of alternatives to such proposal actually considered by the United States.

(c) The United States shall also cause to be published, commencing at least 60 days prior to the effective date of the judgment described in subsection (b) of this section, for 7 days over a period of 2 weeks in newspapers of general circulation of the district in which the case has been filed, in the District of Columbia, and in such other districts as the court may direct —

(i) a summary of the terms of the proposal for the consent judgment,

(ii) a summary of the competitive impact statement filed under subsection (b) of this section,

(iii) and a list of the materials and documents under subsection (b) of this section which the United States shall make available for purposes of meaningful public comment, and the place where such materials and documents are available for public inspection.

(d) During the 60-day period as specified in subsection (b) of this section, and such additional time as the United States may request and the court may grant, the United States shall receive and consider any written comments relating to the proposal for the consent judgment submitted under subsection (b) of this section. The Attorney General or his designee shall establish procedures to carry out the provisions of this subsection, but such 60-day time period shall not be shortened except by order of the district court upon a showing that (1) extraordinary circumstances require such shortening and (2) such shortening is not adverse to the public interest. At the close of the period during which such comments may be received, the United States shall file with the district court and cause to be published in the Federal Register a response to such comments.

(e) Before entering any consent judgment proposed by the United States under this section, the court shall determine that the entry of such judgment is in the public interest. For the purpose of such determination, the court may consider —

(1) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration or relief sought, anticipated effects of alternative remedies actually considered, and any other considerations bearing upon the adequacy of such judgment;

(2) the impact of entry of such judgment upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

(f) In making its determination under subsection (e) of this section, the court may —

(1) take testimony of Government officials or experts or such other expert witnesses, upon motion of any party or participant or upon its own motion, as the court may deem appropriate;

(2) appoint a special master and such outside consultants or expert witnesses as the court may deem appropriate; and request and obtain the views, evaluations, or advice of any individual, group or agency of government with respect to any aspects of the proposed judgment or the effect of such judgment, in such manner as the court deems appropriate;

(3) authorize full or limited participation in proceedings before the court by interested persons or agencies, including appearance amicus curiae, intervention as a party pursuant to the Federal Rules of Civil Procedure, examination of witnesses or documentary materials, or participation in any other manner and extent which serves the public interest as the court may deem appropriate;

(4) review any comments including any objections filed with the United States under subsection (d) of this section concerning the proposed judgment and the responses of the United States to such comments and objections; and

(5) take such other action in the public interest as the court may deem appropriate.

(g) Not later than 10 days following the date of the filing of any proposal for a consent judgment under subsection (b) of this section, each defendant shall file with the district court a description of any and all written or oral communications by or on behalf of such defendant, including any and all written or oral communications on behalf of such defendant, or other person, with any officer or employee of the United States concerning or relevant to such proposal, except that any such communications made by counsel of record alone with the Attorney General or the employees of the Department of Justice alone shall be excluded from the requirements of this subsection. Prior to the entry of any consent judgment

pursuant to the antitrust laws, each defendant shall certify to the district court that the requirements of this subsection have been complied with and that such filing is a true and complete description of such communications known to the defendant or which the defendant reasonably should have known.

(h) Proceedings before the district court under subsections (e) and (f) of this section, and the competitive impact statement filed under subsection (b) of this section, shall not be admissible against any defendant in any action or proceeding brought by any other party against such defendant under the antitrust laws or by the United States under section 15a of this title nor constitute a basis for the introduction of the consent judgment as prima facie evidence against such defendant in any such action or proceeding.

(i) Whenever any civil or criminal proceeding is instituted by the United States to prevent, restrain, or punish violations of any of the antitrust laws, but not including an action under section 15a of this title, the running of the statute of limitations in respect of every private or State right of action arising under said laws and based in whole or in part on any matter complained of in said proceeding shall be suspended during the pendency thereof and for one year thereafter: *Provided, however*, That whenever the running of the statute of limitations in respect of a cause of action arising under section 15 or 15c of this title is suspended hereunder, any action to enforce such cause of action shall be forever barred unless commenced either within the period of suspension or within four years after the cause of action accrued.

*15 U.S.C. § 29:*

(a) Except as otherwise expressly provided by this section, in every civil action brought in any district court of the United States under the Act entitled "An Act to protect trade and commerce against unlawful restraints and monopolies", approved July 2, 1890, or any other Acts having like purpose that have been or hereafter may be enacted, in which the United States is the complainant and equitable relief is sought,

any appeal from a final judgment entered in any such action shall be taken to the court of appeals pursuant to sections 1291 and 2107 of Title 28. Any appeal from an interlocutory order entered in any such action shall be taken to the court of appeals pursuant to sections 1292(a)(1) and 2107 of Title 28 but not otherwise. Any judgment entered by the court of appeals in any such action shall be subject to review by the Supreme Court upon a writ of certiorari as provided in section 1254(1) of Title 28.

(b) An appeal from a final judgment pursuant to subsection (a) of this section shall lie directly to the Supreme Court if, upon application of a party filed within fifteen days of the filing of a notice of appeal, the district judge who adjudicated the case enters an order stating that immediate consideration of the appeal by the Supreme Court is of general public importance in the administration of justice. Such order shall be filed within thirty days after the filing of a notice of appeal. When such an order is filed, the appeal and any cross appeal shall be docketed in the time and manner prescribed by the rules of the Supreme Court. The Supreme Court shall thereupon either (1) dispose of the appeal and any cross appeal in the same manner as any other direct appeal authorized by law, or (2) in its discretion, deny the direct appeal and remand the case to the court of appeals, which shall then have jurisdiction to hear and determine the same as if the appeal and any cross appeal therein had been docketed in the court of appeals in the first instance pursuant to subsection (a) of this section.

Supreme Court, U.S.
FILED
NOV 23 1983
ALEXANDER L. STEVAS
CLERK

Nos. 83-737 and 83-738

# In the Supreme Court of the United States

OCTOBER TERM, 1983

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PEOPLE OF THE STATE OF CALIFORNIA, ET AL.,
APPELLANTS

*v.*

UNITED STATES OF AMERICA, ET AL.

---

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,
APPELLANT

*v.*

UNITED STATES OF AMERICA, ET AL.

---

*ON APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA*

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## MOTION TO AFFIRM

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REX E. LEE
*Solicitor General*
WILLIAM F. BAXTER
*Assistant Attorney General*
BARRY GROSSMAN
ROBERT B. NICHOLSON
NANCY C. GARRISON
*Attorneys*

*Department of Justice*
*Washington, D.C. 20530*
*(202) 633-2217*

## QUESTION PRESENTED

Whether the district court abused its discretion in approving, as consistent with the provisions and principles of the modified consent decree, the plan of reorganization agreed to by AT&T and the government, which specifies in greater detail how that consent decree is to be implemented.

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# In the Supreme Court of the United States

OCTOBER TERM, 1983

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No. 83-737

PEOPLE OF THE STATE OF CALIFORNIA, ET AL., APPELLANTS

*v.*

UNITED STATES OF AMERICA, ET AL.

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No. 83-738

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE, APPELLANT

*v.*

UNITED STATES OF AMERICA, ET AL.

---

*ON APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA*

---

## MOTION TO AFFIRM

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### OPINIONS BELOW

The August 11, 1982, opinion of the district court (J.S. App. 1-172) and the modification of final judgment (J.S. App. 173-190) filed August 24, 1982, are officially reported as *United States* v. *AT&T*, 552 F. Supp. 131 aff'd mem. *sub nom. Maryland* v. *United States*, No. 82-952 (Feb. 28, 1983).

The July 8, 1983, opinion of the district court stating that it would approve the plan of reorganization only if

modified in certain respects (J.S. App. 195-330) is reported at 569 F. Supp. 1057-1124. The July 28 and August 5, 1983, memoranda of the district court clarifying and denying reconsideration of the July 8 opinion (J.S. App. 331-340, 341-348) are reported at 569 F. Supp. 1124-1131. The order entered August 5, 1983, approving the plan of reorganization as amended (J.S. App. 349-350) is reported at 569 F. Supp. 1131. The September 7, 1983 order of the district court granting certification to this Court under 15 U.S.C. 29(b) (J.S. App. 351-354) is not yet reported.

## JURISDICTION

The order approving the plan of reorganization was entered on August 5, 1983 (J.S. App. 349-350). The notice of appeal of the People of the State of California and the Public Utilities Commission of the State of California was filed on August 10, 1983 (J.S. App. 355-356). On September 7, 1983, the district court certified that the direct consideration by this Court of all appeals in this case is of general public importance in the administration of justice (J.S. App. 351-354). On September 13, 1983, the New York State Department of Public Service filed a notice of appeal (J.S. App. 357-358). The appeals were docketed in this Court on November 2 and 3, 1983. The jurisdiction of this Court is invoked under 15 U.S.C. 29(b).

## STATEMENT

1. On January 8, 1982, the government and the American Telephone & Telegraph Company (AT&T) announced the dismissal of the government's pending antitrust case against the company.[1] Concurrently,

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[1] The government sued AT&T in 1974, claiming that AT&T had used its monopoly power in local exchange telephone service to exclude competition in the telecommunications equipment and intercity services markets, in violation of Section 2 of the Sherman Act, 15 U.S.C. 2. *United States* v. *American Tele-*

they announced a proposed modification of a 1956 consent decree entered in an earlier suit[2] which provided all of the relief sought by the government in the 1974 litigation. Specifically, it provided for the separation of the Bell operating companies, which provide local telephone services, from the remainder of the AT&T system. J.S. App. 174-175. This separation would eliminate AT&T's ability to continue the anticompetitive practices alleged in both cases by preventing AT&T from employing monopoly power in local exchange services to disable competition in other, potentially competitive markets.[3] The decree further required that, not

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phone & Telegraph Co., Civ. No. 74-1698 (D.D.C. filed Nov. 20, 1974). In particular, the complaint alleged that AT&T had monopolized customer premises equipment (CPE) by discriminating against competitors' equipment, had monopolized telecommunications equipment used by the Bell operating companies (BOCs) through various preferential devices, and had monopolized intercity telecommunications through discriminatory terms imposed upon and discriminatory refusals to interconnect with other companies. At trial, the government sought the divestiture of those parts of the BOCs that provide local exchange services, or, alternatively, divestiture of Western Electric.

[2] In 1949, the United States sued Western Electric Company, Inc., and its parent, AT&T, claiming that they had monopolized and conspired to restrain trade in the manufacture and distribution of telephone equipment, in violation of Sections 1 and 2 of the Sherman Act, 15 U.S.C. 1 and 2. *United States* v. *Western Electric Co.*, Civ. No. 17-49 (D.N.J. filed Jan. 14, 1949).

[3] The 1956 consent decree prohibited AT&T and the BOCs from engaging "in any business other than the furnishing of common carrier communications services," defined as "services and facilities * * * the charges for which are subject to public regulation under the Communications Act of 1934" or under state law. See J.S. App. 7, 81 n. 196. The decree also required the licensing of Bell System patents to all applicants at reasonable royalties. *Id.* at 7, 77. Because the new structural relief provided by the modified decree renders these restraints unnecessary, the decree frees AT&T from these restrictions. See generally *id.* at 57-58, 66-67.

later than six months after its effective date, AT&T submit to the Department of Justice for its approval a plan of reorganization to implement the decree, such plan to be effective not later than 18 months after the date of the decree. *Id.* at 174.

On August 11, 1982, following extensive comments, briefing and argument by interested parties,[4] the district court issued a lengthy opinion in which it found that most of the provisions of the proposed modified decree, including the basic provision for AT&T's divestiture of the BOCs' local exchange monopolies, were in the public interest (J.S. App. 1-172).[5] The district court stated, however, that it would approve the decree only if the parties agreed to several substantive and procedural amendments to the proposed decree (*id.* at 170-172). Among these was a provision specifying that the plan of reorganization to be prepared by AT&T and approved by the Department of Justice would "not be implemented until approved by the [district c]ourt as being consistent with the provisions and principles of the decree" (*id.* at 156, 172). The government and

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[4] The United States published notice of the proposed settlement and a competitive impact statement in the Federal Register. 47 Fed. Reg. 7170-7184 (1982). The district court received more than 600 comments on the proposed modified decree and numerous briefs on several issues from more than 100 organizations. See J.S. App. 22-25. It also heard oral argument at which 20 counsel from 18 organizations participated (*id.* at 25 & n.65).

[5] Over the objections of several states and state regulatory agencies, the court held that, in order to effectuate the decree's goal of eliminating the effects of past anticompetitive conduct in interstate communications, it could order AT&T to take actions, such as reorganizing and separating assets and common carrier responsibilities, without obtaining prior approval of such actions from state regulatory agencies (J.S. App. 36-48). The court also approved releasing AT&T from most of the line-of-business restrictions and patent licensing requirements imposed by the 1956 decree (*id.* at 77-79).

AT&T thereafter agreed to the court's proposed changes, and on August 24, 1982, the court entered the decree as a modification of the 1956 final judgment in the *Western Electric* case (*id.* at 173-190).[6]

2. The district court allowed numerous states, state regulatory agencies, and private parties to intervene in the proceedings (J.S. App. 191-194), and several of these intervenors noticed appeals from the judgment. On November 10, 1982, the district court, pursuant to the Expediting Act, 15 U.S.C. 29(b), certified the appeals for immediate review by this Court, finding that "immediate consideration of the appeal by the Supreme Court is of general public importance in the administration of justice." See J.S. App. 352-353. As requested by the United States and AT&T, this Court accepted jurisdiction of the appeals and summarily affirmed the decree. *Maryland* v. *United States*, No. 82-952 (Feb. 28, 1983).

3. On December 16, 1982, AT&T submitted a proposed plan of reorganization to the Department of Justice. The Department carefully reviewed the 471-page plan and discussed it with state regulatory officials, other carriers, providers of telecommunications equipment, officials of AT&T and the BOCs, and others. U.S. Resp. at 14-20.[7] As a result of its review, the Department required AT&T to make various modifications and, as modified, the plan was submitted to the district court. J.S. App. 195-196. The court thereafter received comments and briefs filed by intervenors and other interested persons, considered the replies of AT&T and

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[6] Because this decree provided all the relief sought in the 1974 litigation, the court accepted a stipulated dismissal of that case.

[7] "U.S. Resp." refers to the Response of the United States to Public Comments and Action on AT&T's Proposed Plan of Reorganization, filed in the district court on March 24, 1983.

the Department of Justice, and heard oral argument on certain issues. *Id.* at 196-197, 323.

On July 8, 1983, the district court issued a lengthy opinion (J.S. App. 195-330) discussing the proposed plan. The court found that most of the provisions of the plan, including the basic plan for division of assets between AT&T and its subsidiaries and for the eventual provision by the BOCs of equal exchange access for all interexchange carriers, were consistent with the provisions and principles of the decree (*id.* at 197). The district court stated, however, that it would require certain modifications in the plan before approving it (*id.* at 197, 328-330). Following AT&T's and the government's consent to these modifications, the court, on August 5, 1983, entered an order approving the plan as modified (*id.* at 349-350).

4. On August 10, 1983, the People of the State of California and the Public Service Commission of the State of California filed a notice of appeal from the order aproving the plan (J.S. App. 355-356). On August 25, 1983, the United States, supported by AT&T, asked the district court to certify the California appeal and any other appeals for direct review by this Court pursuant to the Expediting Act. No party opposed that request.

On September 7, 1983, the district court certified the appeals, finding that the considerations that had supported direct Supreme Court review of the appeals from the entry of the decree were equally applicable to review of the order approving the plan (J.S. App. 351-354). The court concluded that "[e]ven though it is not likely that the appeals will present questions of legal significance, they are clearly of general public importance" (*id.* at 352) (footnote omitted) because AT&T's divestiture of the BOCs, "apparently the largest corporate reorganization in history, will directly affect millions of employees and shareholders, the na-

tion's telephone subscribers, AT&T's competitors, the telecommunications industry in general, and the responsibilities of federal and state regulatory bodies" (*id.* at 353). Moreover, the district court noted, given the rapidly approaching January 1, 1984, divestiture date, "a speedy, final resolution of the legal situation is all the more necessary" to protect the public interest as well as "the various private interests involved" in the divestiture *(ibid.)*. Accordingly, since "[i]t is unlikely that such a resolution could be secured through the normal process of review by the U.S. Court of Appeals to be followed by a petition for writ of certiorari to the Supreme Court" *(ibid.)*, the district court certified that "immediate consideration * * * of the appeal and of any additional appeals filed hereafter is of general public importance in the administration of justice" (*id.* at 354) (footnote omitted).[8]

## ARGUMENT

Last Term, this Court summarily affirmed the modified consent decree entered by the district court in this case. Thus, the Court is familiar with the provisions and principles of the decree and is well aware that its prompt implementation is "of general public importance in the administration of justice" (15 U.S.C. 29(b)). The plan of reorganization, which is the subject of the present appeals, actuates the provisions of the decree, and the policies that justified expedited review last Term are fully applicable here. Moreover, as in the earlier appeal, the issues now before the Court do not warrant

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[8] The New York State Department of Public Service subsequently filed a notice of appeal on September 13, 1983. J.S. App. 357-358. No other party has appealed.

All appeals from the order approving the plan must be taken directly to this Court; the court of appeals has no jurisdiction absent a remand pursuant to 15 U.S.C. 29(b)(2). *United States* v. *Western Electric Co.*, 714 F.2d 178 (D.C. Cir. 1983).

plenary consideration. Accordingly, the United States, pursuant to the Expediting Act, 15 U.S.C. 29(b), and Rule 16.1 of the Rules of this Court, moves for summary affirmance.

## I. THE COURT SHOULD ACCEPT THE DIRECT APPEALS

The appropriateness of direct review under the Expediting Act, 15 U.S.C. 29(b), turns on the importance of a prompt decision of a case in view of its economic significance, not on the difficulty or general significance of the legal issues presented. The Act expressly refers to the importance of "immediate consideration of the appeal" and makes no mention of the significance of the issues raised.[9] Similarly, the focus of the legislative history of the Expediting Act[10] is not on the importance of the issues raised to the development of the law, but rather on the immediate economic impact of the case itself.[11] While Congress, of course, did not regard every

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[9] Prior to 1974, the Expediting Act, ch. 544, 32 Stat. 823 *et seq.*, provided for direct review by this Court in all government civil antitrust suits. The Act was amended to its present form in 1974 to relieve this Court of that burden. See S. Rep. 93-298, 93d Cong., 1st Sess. 6 (1973). In amending the statute, however, Congress recognized that occasionally there would be antitrust cases for which the public interest required an avenue of direct appeal to this Court. Accordingly, Congress preserved a limited right of direct appeal under 15 U.S.C. 29(b).

[10] See generally S. Rep. 93-298, 93d Cong., 1st Sess. 7-8 (1973); H.R. Rep. 93-1463, 93d Cong., 2d Sess. 10-11 (1974); 119 Cong. Rec. 24599 (1973); 120 Cong. Rec. 38585-38587, 39123 (1974).

[11] As the House Judiciary Committee noted in its report on this provision, "public antitrust cases are unlike other federal cases, * * * they have an impact on the economic welfare of this nation, and * * * consequently they should be treated accordingly." H.R. Rep. 93-1463, 93d Cong., 2d Sess. 14 (1974). See also S. Rep. 93-298, 93d Cong., 1st Sess. 3-4 (1973); 119 Cong. Rec. 24599 (1973).

government civil antitrust suit as being sufficiently important to merit direct review, it did establish a mechanism by which antitrust cases with the most significant economic impact on the public interest could be appealed directly to this Court. This case satisfies that admittedly high standard.

A. The consent decree in this case provides an effective structural remedy that will further the public interest in competition and remedy past competitive restraints in the vitally important national telecommunications industry. As the district court and this Court recognized, direct review of the decree was necessary to minimize delay in the development of the plan of reorganization and uncertainty as to when—and, indeed, whether—the actions required by the decree would occur. Such delay or uncertainty would have been harmful not only to AT&T, its employees, shareholders, and customers, but also to other firms in the telecommunications and related industries, whose business plans depend on the divestiture schedule. Most importantly, delay would have been harmful to the public interest in speedily ending restraints on competition and establishing a restructured, competitive telecommunications industry.[12] It was for these reasons that the district court certified and this Court accepted expedited consideration of the decree.

B. The plan of reorganization approved by the district court is the essential blueprint for implementation of the decree. Accordingly, the district court correctly concluded (J.S. App. 352) that the same considerations that made expedited review of the decree appropriate are equally applicable to appeals calling into question the validity of the plan; progress toward implementa-

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[12] Expedited direct review of the decree also served to minimize the risk that states would obtain court orders conflicting with or enjoining actions essential to the decree's implementation.

tion of the decree has not lessened the significance of this case. As the district court emphasized in certifying these appeals (*id.* at 353), the plan implements the divestiture mandated by the decree, which is "the largest corporate reorganization in history [and which] will directly affect millions of employees and shareholders, the nation's telephone subscribers, AT&T's competitors, the telecommunications industry in general, and the responsibilities of federal and state regulatory bodies." Since "the various public and private bodies are currently implementing detailed plans to effectuate the reorganization" on the January 1, 1984, date prescribed in the plan, "[u]ncertainty regarding the legal status of [the] reorganization would have serious adverse consequences" for all the diverse interests involved (*ibid.*) (footnote omitted)—adverse consequences that can be avoided by a final ruling by this Court. Such review must be expedited because it is even more clear than it was a year ago that the normal process of appellate review will not permit such a ruling before January 1, 1984, the date of implementation of the plan.[13]

C. Direct review is particularly appropriate in this case in light of the nature of the issues raised by appellants. They have challenged provisions of the plan which, as AT&T explains (Mot. to Aff. 11), have significant financial implications for AT&T, the BOCs, and various regulatory authorities. As a result, the mere pendency of the appeals—despite their lack of merit—creates uncertainty not only for BOC and AT&T managements, but also for the regulators and the millions of investors, potential investors, creditors and ratepayers affected by this case. This Court, having previously re-

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[13] Even if this Court is unable to rule before January 1, 1984, an expedited decision in this Court will better serve the public interest in the prompt resolution of this case than would a remand to the court of appeals, as suggested by appellants (Cal. J.S. 21).

viewed the decree, is familiar with its provisions and principles. Consequently, direct review of the meritless issues raised by California and the New York Department of Public Service should not be unduly burdensome for the Court, particularly when weighed against the public benefit that will result from an expeditious resolution of this exceedingly important case.

## II. THE COURT SHOULD SUMMARILY AFFIRM THE JUDGMENT OF THE DISTRICT COURT

The appellants' claims that certain aspects of the plan of reorganization are inconsistent with the modified consent decree are insubstantial and do not warrant plenary consideration.

### A. The District Court's Judgment Must Be Affirmed Unless There Has Been A Clear Abuse of Discretion

This Court has affirmed the modified consent decree itself, and appellants cannot and do not challenge the decree's provisions. The government and AT&T, moreover, agree that the plan is consistent with the obligations imposed on AT&T by the decree. Thus, were this a normal case, there would be no need for judicial intervention.[14] But, because of the complexity and importance of this case, the district court insisted that the plan "not be implemented until approved by the [district c]ourt as being consistent with the provisions and principles of the decree" (J.S. App. 152-156, 169-170, 172). The district court has approved the plan, and its determination, contested by appellants, should be given substantial deference by this Court.

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[14] A consent decree has attributes of both a contract and a judicial act (*United States* v. *ITT Continental Baking Co.*, 420 U.S. 223, 236 n.10 (1975)), but it "is to be construed for enforcement purposes basically as a contract" (*id.* at 238). Accord, *United States* v. *Armour & Co.*, 402 U.S. 673 (1971). Like any other contract, a consent decree is properly viewed as an embodiment of the intent of the parties.

The district court found the plan to be consistent with the provisions and principles of the modified consent decree after careful consideration of the extensive submissions by the parties and intervenors.[15] The officials of the newly created regional operating companies, furthermore, represented to the court that the plan (amended as required by the government and the district court) will enable them to be economically and functionally viable, and the vast majority of the intervenors, notwithstanding their diverse interests, now appear willing to accept the plan. Significantly, there is no dispute between the parties to the decree as to its meaning. In these circumstances, deference to the district court's conclusion that the plan is consistent with the decree is peculiarly appropriate and, absent a showing that the district court clearly abused its discretion,[16] the district court's judgment should be affirmed.

**B. The Plan's Allocation of Account 232 Assets Is Consistent with the Decree**

The central purpose of the modified consent decree is to prevent the recurrence of the anticompetitive conduct alleged in this litigation by separating those parts of the Bell operating companies that provide exchange telecommunications and exchange access services, which presently constitute a series of monopoly markets, from the rest of the Bell System. Thus, the decree

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[15] In the exercise of its oversight function, the district court, which had carefully scrutinized the decree itself, received and considered over 50 sets of comments on the plan from interested persons as well as the responses of the Department of Justice and AT&T, and the statements of officials of the new regional BOCs. See J.S. App. 195-197, 323.

[16] Clear abuse of discretion is the appropriate standard for appellate review of a district court's determination that a consent decree is in the public interest. See, *e.g.*, *Cranston* v. *Hardin*, 504 F.2d 566, 577 (2d Cir. 1974); *City of Detroit* v. *Grinnell Corp.*, 495 F.2d 448, 454-455 (2d Cir. 1974).

provides that the divested BOCs will retain "all facilities, personnel and books of account * * * relating to the exchange telecommunications or exchange access functions" (as defined in the decree) (J.S. App. 174). In addition, the BOCs will receive from AT&T and its affiliates "sufficient facilities, personnel, systems, and rights to technical information" to permit the BOCs to perform those functions independently of AT&T (*ibid.*). AT&T is to retain those "facilities, personnel and books of account * * * relating to other functions (including the provision of interexchange switching and transmission and the provision of customer premises equipment to the public)" (*ibid.*).[17]

Dividing over $150 billion in Bell System assets and corresponding liabilities according to these principles is obviously a complex task. While the government, the district court and most interested persons have concluded that the plan will accomplish this task in a manner consistent with the decree, California and the New York Department of Public Service would each prefer a slightly different allocation of assets. The changes in the plan that each of these appellants advocates would appear to benefit its own local ratepayers over other users of or investors in the national telecommunications system. But that obviously is not a purpose of the decree, and neither appellant can show any abuse of discretion in the district court's approval of the plan.

One category of assets assigned to the BOCs under the plan consists of all assets included in Account 232 of the Federal Communications Commission's Uniform System of Accounts. The Commission defines Account 232 to include "the original cost of installing or connecting items of station apparatus and the original cost of inside wiring and cabling and of drop and block

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[17] The decree allows the BOCs to provide, but not to manufacture, CPE (J.S. App. 183).

wires." 47 C.F.R. 31.232(a). Account 232, in other words, comprises the capitalized cost of connecting telephone equipment on a customer's premises to the local exchange. While appellants agree that some portion of Account 232 should be assigned to the BOCs (see Cal. J.S. 11-13, 15; N.Y. J.S. 5-6), they contend that the "station handling costs" included in this account should instead be assigned to AT&T (Cal. J.S. 11-13; N.Y. J.S. 5-6). California (but not the New York DPS) also contends that "complex intrasystem wiring" should be transferred to AT&T (Cal. J.S. 14-18). Appellants, however, have failed to show that the assignment of the entire Account 232 to the BOCs is inconsistent with the decree.

1. Under FCC accounting procedures, capitalized labor costs associated with the installation and testing of customer premises equipment (CPE), sometimes referred to as "station handling costs," are included as an undifferentiated portion of Account 232. See 47 C.F.R. 31.232. Appellants argue (Cal. J.S. 12; N.Y. J.S. 5) that the plan's assignment of these costs to the BOCs violates the decree's requirement that AT&T retain all "books of account * * * relating to * * * the provision of customer premises equipment to the public" (J.S. App. 174). California also argues (Cal. J.S. 12) that this assignment is inconsistent with the functional separation of assets mandated by the decree because station handling costs relate to CPE, which is an AT&T function under the decree, rather than to the BOCs' exchange functions.

The district court acknowledged (J.S. App. 344) that "a theoretical case could be made" for assignment of station handling costs to AT&T. However, as the court also recognized (*id.* at 344 n.9), the regulatory principles that have governed the recovery of station handling costs have associated them primarily with the growth of the local exchange as a whole rather than

with particular customers. Prior to 1981, it was the Federal Communications Commission's policy to capitalize station handling costs as part of Account 232 and to allow their recovery through rates to all subscribers. The rationale for this regulatory policy was that this method of accounting and recovering the investment in labor costs would make telephone service more affordable and, as a result, increase the value of telephone service for all subscribers by expanding the total subscriber base.[18] When the FCC changed its accounting system to require that station handling costs in the future be expensed rather than capitalized, it provided that embedded investment, which in essence represents a "loan" to all customers to finance the growth of the telephone system, would be recovered over a 10-year period through the rates to those customers.[19] Accordingly, it is consistent with the decree's functional separation provisions and principles to assign accrued station handling costs to the BOCs, which, in accordance with FCC regulatory policy, will be able to continue to recover them from the general body of ratepayers. Since all ratepayers received the benefits associated with the capitalization of these costs, such a result is not, as California contends (Cal. J.S. 13), unfair to "the ratepaying public."

Moreover, as noted by the district court (J.S. App. 344), there is no way to segregate retroactively the time spent connecting CPE from time spent on non-CPE installation work (see AT&T Mot. to Aff. 17). Contrary to California's contention (Cal. J.S. 13), the Department of Justice did not simply accept AT&T's statement on this matter. Rather, the Department investigated in some detail the possibility of segregating

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[18] See *In re AT&T*, 64 F.C.C. 2d 1, 54-55, 354-355 (1977).

[19] *In re Amendment of Part 31, Uniform System of Accounts*, 85 F.C.C. 2d 818, 828-829 (1981).

CPE installation costs and the Department (see U.S. Resp. 91 n.*), as well as the district court (see J.S. App. 344), was persuaded that accurate segregation of these costs is indeed impractical.[20]

The New York DPS's contention (N.Y. J.S. 7) that, by not assigning the accrued station handling costs to AT&T, the plan gives AT&T some unfair advantage in CPE competition also misses the mark. The assignment of station handling costs will not affect AT&T's CPE prices. Those prices will be determined by CPE costs and competitive factors. In a competitive environment, AT&T would not be able to raise CPE prices above CPE costs to recoup past station handling costs (or any other non-CPE cost), since customers would simply buy from AT&T's competitors if it did so. In other words, capitalized past costs are an "asset" to regulated companies only because regulatory policies allow them to be recovered from ratepayers. In a competitive market, these kinds of capitalized installation costs are simply a kind of "bad debt." Thus, if station handling costs were assigned to AT&T, it, unlike the BOCs, could not recover them and likely would have no alternative but to write them off as a loss. Therefore, to assign these costs to AT&T would be inconsistent with established regulatory policy and unfair to AT&T's investors and creditors.[21]

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[20] California contends (Cal. J.S. 13) that "the BOCs in California and New York had already separated all the various elements of Account 232 and that other states would not find it difficult to do the same." The Department concluded, however, that the procedures used in these states could not necessarily be applied in other states and an attempt to segregate Account 232 costs was not, in any event, required by the decree.

[21] Moreover, there is no indication in any statements by the parties or the district court that the assumption of this debt by AT&T was an intended result of the decree, and it would not further competition in any way.

2. Wiring that connects two pieces of customer premises equipment is referred to as "complex intrasystem wiring." It, like station handling costs, is included in asset Account 232. Contrary to California's contentions (Cal. J.S. 14), this wiring is not CPE, nor is it "related to" the provision of CPE within the meaning of the decree. Thus, assignment of this portion of Account 232 to the BOCs also was proper.

California's contention (Cal. J.S. 14) that the decree's definition of CPE "clearly embraces complex inside wiring" is based on a reading of the decree language that fails to take into account the intention of the parties as evidenced by their statements to the district court. The decree defines CPE as "equipment employed on the premises of a person (other than a carrier) to originate, route, or terminate telecommunications" (J.S. App. 177). The government's February 1982 Competitive Impact Statement, filed with the court to explain the meaning and intended effect of the decree, stated (47 Fed. Reg. 7180) that the decree's "structural separation of competitive and noncompetitive markets is consistent with recent regulatory decisions," and specifically cited (*id.* at 7180 n.31) the FCC's *Computer II* decisions, in which the FCC excluded inside wiring (both simple and complex) from the category of CPE.[22]

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[22] See, *e.g.*, *In re Amendment of Section 64.702 of the Commission's Rules & Regulations (Second Computer Inquiry)*, 84 F.C.C. 2d 50, 61 n.10 (1980). Although the FCC currently is considering the deregulation of inside wiring in two proceedings (*Modifications to the Uniform System of Accounts*, 47 Fed. Reg. 44770 (1982); *In re Deregulation of Customer Premises Inside Wiring*, 86 F.C.C. 2d 885 (1981)), it has not classified this wiring as CPE. Moreover, for purposes of construing the decree, subsequent regulatory definitions of CPE are of limited relevance. Rather, the district court properly looked to the FCC's treatment of CPE at the time of the parties' reference to it.

In addition, when the provisions of the plan assigning complex inside wiring to the BOCs were challenged in the district court, the parties emphasized that they intended to follow the FCC's definition of CPE (U.S. Resp. 87; AT&T Resp. 157-158[23]). They added that, in defining CPE to include equipment used to "route" calls, they did not intend to include inside wire (U.S. Resp. 87-88; AT&T Resp. 157-158). Rather, they understood equipment used to "route" telecommunications to refer to equipment that performs a switching function, such as a private branch exchange. Although inside wiring transmits telecommunications, it is not "equipment" and does not "route" calls within the parties' understanding of those terms (U.S. Resp. 88; AT&T Resp. 156-157). The district court, having considered these factors, properly concluded that assignment of inside wiring to the BOCs is consistent with the decree's definition of CPE (J.S. App. 344).

California's argument that, even if inside wiring is not CPE, it should nevertheless be assigned to AT&T because it is "related to" the provision of CPE (Cal. J.S. 14) expands the term "related to" beyond the intent of the parties and ignores the underlying division of assets effected by the decree itself. As the parties explained to the district court (U.S. Resp. 87 n.*; AT&T Resp. 157 n.*), assets "relating to" CPE include separate ancillary assets (*e.g.*, motor vehicles, tools and other work equipment) that are associated with the provision of CPE, but do not include all assets that are "connected to" CPE. Indeed, were California's "connected to" interpretation correct, the wires from customers' premises to the BOCs' central offices also would be "related to" CPE and assigned to AT&T—a

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[23] "AT&T Resp." refers to AT&T Response to Objections to Its Proposed Plan of Reorganization, filed in the district court on March 14, 1983.

result clearly at odds with the provisions and principles of the decree.

Despite California's submission (Cal. J.S. 15), there is no inconsistency between the assignment of complex inside wiring to the BOCs and the fundamental competitive principles underlying the decree.[24] To the contrary, as the district court expressly concluded in rejecting arguments that portions of Account 232 should be assigned to AT&T (J.S. App. 344) (footnote omitted):

> In-place wiring, which is a principal item in Account 232, is as much a "bottle-neck" as are the subscriber access lines. To assign such wiring to AT&T would be to insert AT&T-controlled facilities between the Operating Companies and the subscribers, and such an assignment would thus be entirely inconsistent with the basic purposes of the decree.

Because the assignment of complex inside wiring to the BOCs furthers the decree's competitive objectives, this aspect of the plan was not only approved by the Department of Justice, but was strongly endorsed by the North American Telephone Association, an associa-

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[24] California also argues (Cal. J.S. 15) that it is unfair to local ratepayers to assign inside wiring to the BOCs because "investment in complex intrasystem wiring is now being recovered in part through equipment rates to business customers," who should continue to pay for it "as part of the complex CPE rate" that will be paid to AT&T by users of its CPE. As the government and AT&T explained to the district court, however, it is not clear to what extent the inside wiring investment in Account 232 is currently recovered through rates for embedded CPE; in many jurisdictions the rates for embedded CPE do not recover any portion of the investment in inside wiring or any other component of Account 232 (U.S. Resp. 89-90; AT&T Resp. 162-163). Moreover, after divestiture the BOCs will continue to have available a number of revenue sources for the recovery of these amounts, and there is nothing in the decree that precludes the BOCs from recovering amounts contained in Account 232 in the form of customer-specific wiring charges. *Ibid.*

tion of CPE manufacturers and suppliers that compete with AT&T. Initial Comments of North American Telephone Association at 21-22. The Kansas regulatory commission also specifically supported it (Comments of Kansas Corporation Commission at 2), and only California has challenged it on appeal.

### C. The Plan's Allocation of Debt Is Consistent With the Decree

Under the plan, Pacific Telephone's embedded cost of funded debt will be approximately 9.5% (AT&T Mot. to Aff. 21, 24). The next highest embedded cost of funded debt for a BOC is Southwestern Bell's 9.4% (*id.* at 22). The Bell system average embedded cost of funded debt is approximately 8.8% (*id.* at 25 n.23). California claims (Cal. J.S. 18-20) that the plan's allocation of debt to Pacific Telephone violates the decree's requirement that "the quality of the [BOCs'] debt [at the time of divestiture] shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time" (J.S. App. 184-185).

The next sentence of the decree, however, which California conspicuously fails to mention, expressly provides that "[u]pon application by a party or a BOC, the [district c]ourt may grant an exception to this requirement" (J.S. App. 185). The district court itself required the inclusion of this sentence in the decree (see *id.* at 170-172) to permit non-uniform allocation of embedded debt where "it can be shown that, with respect to a particular Operating Company, its own current debt provides a more equitable basis" (*id.* at 137 n.321). Such a showing was made in the case of Pacific Telephone, and there consequently was no abuse of discretion in the district court's approval of this aspect of the plan.[25]

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[25] California claims (Cal. J.S. 20 n.19) that the district court never granted "a formal exception to the decree." If California is suggesting that the court did not grant an exception to the

As the Department and AT&T explained to the district court (U.S. Resp. 117-122; AT&T Resp. 284-299), several factors contribute to Pacific's higher embedded cost of debt. First, the embedded cost of debt for the three high growth "Sun Belt" regional operating companies (Southern-South Central Bell, Southwestern Bell, and Pacific Telephone) is higher than that for BOCs serving other regions. This difference reflects the fact that the BOCs that serve high growth areas have had more frequent and more recent occasion to go to the debt market to meet their service demands. If each of the seven regional companies were required to be divested with the average cost of debt of the Bell System as a whole, the three Sun Belt regions with their higher embedded cost of debt would, in effect, receive a subsidy from the four regional companies that serve more slowly growing areas. Such subsidies, the parties explained (U.S. Resp. 119; AT&T Resp. 278-281), and the court agreed (J.S. App. 222 n. 64), would have been unfair to the lower growth companies and to their subscribers.

Second, Pacific Telephone's embedded cost of debt is higher than the costs of even other high growth BOCs because its financial condition, as measured by its rate of return, stock price, financial ratios, bond ratings,

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equal debt quality requirement, its argument lacks merit because the court substantively, if not "formally," granted such an exception. The Department and AT&T both requested that the court grant whatever exceptions to the equal debt quality standard were necessary for approval of the plan (U.S. Resp. 119, 122; AT&T Resp. 298), and the court, which expressly referred to Pacific's unique circumstances (J.S. App. 222 n.64), must be understood to have granted whatever exception to that standard was necessary to support its approval of the debt allocation provisions of the plan. If, on the other hand, California is suggesting that some exception to the *decree* itself is necessary, its argument fails because the decree *does* permit the non-uniform allocation of debt approved by the court.

and the views of analysts and investors, had steadily deteriorated between 1973 and 1980 (see J.S. App. 137 n.320; AT&T Resp. 285-299; AT&T Mot. to Aff. 5 n.3, 23-24). Indeed, the modified consent decree explicitly recognizes Pacific Telephone's unique financial situation, and accordingly provides that Pacific Telephone is to be divested with approximately 50% instead of approximately 45% debt, as in the case of the other BOCs (J.S. App. 184; see J.S. App. 137 & n.320).

Moreover, there is nothing in the modified consent decree or any related proceeding to support California's contention (Cal. J.S. 19) that, because the decree expressly provided Pacific Telephone with a less advantageous debt ratio than the other BOCs, the decree's provision for an exception to the equal debt quality standard could not also be applied to Pacific. On the contrary, as a matter of economics, the decree's debt ratio provision supports application of the equal debt quality exception to Pacific. It is the combination of Pacific's higher debt ratio and its lower bond rating that accounts for the difference between Pacific's embedded debt costs and those of the other Sun Belt companies.[26] In these circumstances, a reallocation of embedded debt to give Pacific the systemwide average cost would unfairly impose on other BOC ratepayers or AT&T stockholders costs attributable to factors unique to California. As the district court recognized: "The debt equalization scheme which is proposed by California would inappropriately result in inter-regional subsidies * * *" (J.S. App. 222 n.64).[27]

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[26] In response to objections to this aspect of the plan, AT&T suggested to the district court (AT&T Resp. 285, 297) that the bulk of the difference between Pacific Telephone's embedded cost of debt and the lower debt costs of the other Sun Belt companies is attributable to the downgrading of Pacific's debt between 1973 and 1980 from an "AAA" to an "A−" rating.

[27] Contrary to California's contention (Cal. J.S. 19), there is

Finally, California's argument ignores the fact that, as the district court noted, "neither the decree nor the plan of reorganization adversely affects Pacific's financial condition; if anything, they improved it" (*ibid.*). Indeed, the plan, which was amended in response to the comments of Pacific's management and now has its support, has resulted in significant improvement in Pacific's financial condition. As originally proposed, the plan would have left Pacific with a debt ratio of 50%[28] and an embedded cost of funded debt of 9.7%-9.9% (see AT&T Resp. 295). Under the plan as approved by the district court, however, Pacific is projected to be divested on January 1, 1984, with a 46.5% debt ratio (significantly better than the 50% provided for by the decree) and an embedded cost of funded debt of approximately 9.5% (AT&T Mot. to Aff. 21, 24-25).[29] As a result of the advantages anticipated from the proposed divestiture, Standard & Poor's, on March 28, 1983, raised Pacific's debt rating from A− to A+ (see AT&T Mot. to Aff. 24 n. 22). Thus, as Pacific's management agrees, its financial condition is fully adequate to allow its post-divestiture viability. The district court correctly exercised its discretion in concluding that the embedded debt allocation provisions of the plan are consistent with the provisions and principles of the decree.

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no inconsistency between this allocation and the allocation of contingent antitrust liabilities. As the court noted (J.S. App. 214-215), there were no substantive differences among the BOCs that compelled differential allocation of the contingent antitrust liabilities.

[28] The 50% debt ratio itself represented a reduction from Pacific's 1981 debt ratio of 57%. See AT&T Resp. 267.

[29] See also Amendment to Plan of Reorganization No. 36 (Topic: Long-Term Debt) (April 7, 1983); Second supplemental statement of Donald E. Guinn filed in the district court on April 7, 1983.

## CONCLUSION

The Court should accept the appeals and affirm the judgment of the district court.

Respectfully submitted.

REX E. LEE
*Solicitor General*
WILLIAM F. BAXTER
*Assistant Attorney General*
BARRY GROSSMAN
ROBERT B. NICHOLSON
NANCY C. GARRISON
*Attorneys*

NOVEMBER 1983

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1983

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No. 83-737

PEOPLE OF THE STATE OF CALIFORNIA, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA, ET AL.

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No. 83-738

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE, APPELLANT

v.

UNITED STATES OF AMERICA, ET AL.

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ON APPEALS FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

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MOTION TO EXPEDITE CONSIDERATION

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The Solicitor General, on behalf of the United States, moves to expedite consideration of the jurisdictional statements and motions to affirm in this case.

This is a civil antitrust action brought by the United States, which the district court has certified for direct review by this Court pursuant to the Expediting Act, 15 U.S.C. 29(b). The consent decree entered in this case requires a substantial reorganization of American Telephone & Telegraph Company (AT&T) to provide effective relief for the competitive harms alleged by the government. The district court found the consent decree to be in

the public interest, but required that the plan of reorganization, which details how the decree will be carried out, be submitted for court approval prior to implementation. Last Term, this Court summarily affirmed the consent decree (Maryland v. United States, No. 82-952 (Feb. 28, 1983)) and the present appeals are from the district court's order approving the plan of reorganization as consistent with the provisions and principles of the decree. The reorganization of AT&T pursuant to the plan is scheduled to occur on January 1, 1984.

Appellants' jurisdictional statements were filed November 2 and 3, 1983. The United States and AT&T are today filing motions to affirm. For the reasons set forth in its motion, the United States agrees with AT&T and the district court that immediate consideration of the appeals by this Court is of general public importance in the administration of justice and that this Court should, therefore, accept the direct appeals. Moreover, since the reorganization will occur on January 1, 1984, and delay beyond that date in the resolution of these appeals would have a broad and significant adverse effect on the telecommunications industry, regulatory authorities, and the public in general, it is important that these appeals be decided before that date if possible.

Accordingly, the United States suggests that the jurisdictional statements and motion to affirm be considered by the Court at its next scheduled conference.

Respectfully submitted.

REX E. LEE
Solicitor General

NOVEMBER 1983

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ALEXANDER L. STEVAS,
CLERK

Nos. 83-737 and 83-738

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

*v.*

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,

*Appellees.*

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,

*Appellant,*

*v.*

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,

*Appellees.*

On Appeal From The United States District Court
For The District Of Columbia

## MOTION TO AFFIRM

HOWARD J. TRIENENS*
ALFRED A. GREEN
JIM G. KILPATRIC
FRANCINE J. BERRY
195 Broadway
New York, New York 10007
(212) 393-5111

*Of Counsel:*

SIDLEY & AUSTIN

GEORGE L. SAUNDERS, JR.
JOHN D. ZEGLIS
DAVID W. CARPENTER
DAVID D. HILLER
One First National Plaza
Chicago, Illinois 60603
(312) 853-7000

*Attorneys for Appellees Western Electric Company and American Telephone and Telegraph Company.*

*Counsel of Record

## QUESTIONS RESTATED

The Modification of Final Judgment ("MFJ") was entered in this case, by consent of the parties, in August, 1982, and summarily affirmed by this Court under the Antitrust Expediting Act in February, 1983. Under the MFJ, the Bell System is now completing a massive reorganization in which it will divest its local exchange operations on January 1, 1984. These appeals present legal challenges to the parties' plan for implementing this reorganization and to the District Court's holding that this plan is "consistent with [the MFJ's] principles and provisions." The questions presented are:

1. Whether direct Supreme Court review of these appeals is "of general public importance in the administration of justice" within the meaning of the Antitrust Expediting Act?

2. Whether the MFJ, which is to be interpreted as a contract between the parties, see, *e.g.*, *United States* v. *ITT Continental Baking Co.*, 420 U.S. 223, 238 (1975), can be held to have been misinterpreted by the parties who negotiated, drafted, and agreed to it and by the District Judge who entered it?

3. Whether, in any event, the District Court abused its discretion in approving a reorganization plan that achieves the structural reorganization sought by the Justice Department and rests on a careful balancing of the interests of telephone users, competitors in the industry, the Bell System's one million employees, and its three million shareholders?

## STATEMENT REQUIRED BY RULE 28.1

Appellee Western Electric Company is a wholly-owned subsidiary of appellee American Telephone and Telegraph Company ("AT&T"). AT&T has no parent company. In addition to its wholly-owned subsidiaries, AT&T has ownership interests in the Southern New England Telephone Company, Cincinnati Bell, Incorporated, and the Cuban American Telephone and Telegraph Company. On January 1, 1984, AT&T will divest seven of its wholly-owned subsidiaries: American Information Technologies Corporation, Bell Atlantic Corporation, BellSouth Corporation, NYNEX Corporation, Pacific Telesis Group, Southwestern Bell Corporation, and U S West, Inc.

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Nos. 83-737 and 83-738

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

*v.*

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,

*Appellees.*

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,

*Appellant,*

*v.*

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY and AMERICAN TELEPHONE AND TELEGRAPH COMPANY,

*Appellees.*

On Appeal From The United States District Court
For The District Of Columbia

## MOTION TO AFFIRM

On August 24, 1982, the District Court, with the consent of the parties, entered the Modification of Final Judgment ("MFJ") in this case. This judgment orders a massive structural reorganization of American Telephone and Telegraph Company ("AT&T") and its subsidiaries ("the Bell System"), which is to occur on January 1, 1984. The appeals from the entry of the MFJ were taken directly to this Court under the Antitrust Expediting Act because the District Court found that legal challenges to the reorganization, no matter how insubstantial, created uncertainty which so

imperiled a vital national industry that the earliest possible final disposition of the appeals was a matter of profound "public importance in the administration of justice." 15 U.S.C. § 29(b). This Court ended this potentially crippling "state of limbo" by deciding the appeals during the 1982 term and summarily affirming the District Court. *Maryland* v. *United States*, 103 S. Ct. 1240 (Feb. 28, 1983).

Now, less than two months before the MFJ is to be implemented, two legal challenges to the reorganization have been filed. These are appeals from the District Court's August 5, 1983, order holding that the parties' plan to implement the MFJ is consistent with its provisions and principles. These appeals, too, were certified to this Court under the Antitrust Expediting Act because the Justice Department urged and the District Court found that the public interest requires final disposition of the challenges to the reorganization before January 1, 1984, and that the nation's need for direct Supreme Court review is now, if anything, more compelling than it was nine months ago.

The only way for this Court to put a timely end to the threats to this vital industry is to decide these appeals under the Antitrust Expediting Act before January 1, 1984. But this need not burden this Court or its docket. The fundamental claim of each of the appellants is that the MFJ has been misconstrued both by the parties who negotiated and drafted it and by the District Judge who entered it. Their contentions are frivolous, and the District Court's decision should be summarily affirmed.

## STATEMENT OF THE CASE

Throughout this century, the Bell System has provided integrated, end-to-end telephone service. Its wholly-owned Bell Operating Companies ("BOCs") have franchised monopolies that provide local exchange service. The BOCs own and provide simple and complex telephone instruments ("customer premises

equipment" or "CPE") as well as the wires, cables, and other transmission facilities that run through buildings, streets, and alleys and connect this equipment to local switching facilities. These local facilities originate and terminate long distance calls as well as provide for local exchange calling. The BOCs and the Long Lines Department of AT&T also own and operate interexchange facilities that provide intercity telephone service. The Bell System is technologically integrated; it both manufactures telecommunications equipment for its own use through Western Electric Company and conducts basic telecommunications research through Bell Telephone Laboratories.

In the past four decades, the Justice Department has twice filed civil actions under the Sherman Act which sought major structural reorganizations of the Bell System. In 1949, it filed this action. It led to the entry of a Final Judgment in 1956 which imposed a number of limitations on the services that the integrated Bell System may provide.

In 1974, the Justice Department brought its second action, *United States* v. *AT&T*, No. 74-1698 (D.D.C.). By that time, changes in technology and regulatory policy had introduced competition into major new areas of telecommunications: customer premises equipment, intercity telecommunications service, and emerging information services.[1] However, the provision of local transmission and switching functions not only retained natural monopoly characteristics but entrants in the newly created competitive markets required access to these "bottleneck" facilities to compete effectively. The Justice Department alleged that the Bell System had the opportunity and the incentive to misuse

[1]Technological changes had largely eliminated previous distinctions between regulated telecommunications services and unregulated data processing. These changes not only permitted actual and potential competition between telephone companies and data processing vendors, but also gave rise to claims that the 1956 Judgment prohibited the Bell System from using data processing technologies to enhance its services and, therefore, from continuing its long history of innovation. See J.A. 82 n. 198.

its control over these "essential facilities" to restrain competition in related competitive markets. The Department ultimately sought the divestiture and complete separation of the Bell System's local exchange facilities from its intercity, CPE, and manufacturing businesses. Stipulation Package 82, *United States* v. *AT&T*, No. 74-1698 (D.D.C.). Despite AT&T's vigorous contentions that it had not abused its control of its local exchange monopolies and that the public interest would best be served by maintaining the end-to-end integration of the Bell System, it became increasingly apparent during the pendency of the 1974 case that AT&T's ownership of local exchange facilities would be a source of continuing controversy and uncertainty even if it won *United States* v. *AT&T*.[2]

**The Modification of Final Judgment.** AT&T concluded that the best way to end the continuing antitrust exposure and to obtain freedom from the obsolete constraints of the 1956 Judgment was to agree to the precise structural reorganization that the Justice Department was seeking in the 1974 case. On January 8, 1982, AT&T and the United States stipulated to the entry of a modification of the 1956 Judgment that would require the divestiture of the Bell System's local exchange facilities and vacate the injunctive provisions of the 1956 Judgment. This modification achieved all the Justice Department's antitrust objectives in its four decades of litigation with AT&T.

When the proposed modification was presented to it, the District Court, with the parties' consent, ordered public interest proceedings—which it conducted with great expedition—that went far beyond the requirements of Antitrust Procedures and Penalties Act of 1974, 15 U.S.C. §§16(b)-(h) ("Tunney Act"). These led to an extensive public examination of the pur-

[2]During this period, the FCC and Congress also debated the issues raised by the 1974 case and the 1956 Judgment, and each considered the adoption of onerous regulations, which would apply to AT&T alone, to minimize or eliminate its alleged incentives and ability to suppress competition through control over local monopolies.

pose, meaning, and effect of each of the proposed modification's provisions.

On August 11, 1982, the District Court held that this proposed reorganization of the Bell System was an entirely appropriate antitrust remedy and manifestly in the public interest, provided several changes were made. See J.A. 1-172. Only two are relevant here. First, the court required the addition of a Section VIII(H) to codify the parties' representations as to the divested companies' capital structures. J.A. 171-72. It provides that the divested BOCs may have debt ratios of no greater than approximately 45 percent, except that in the case of Pacific Telephone and Telegraph Company ("Pacific" or "Pacific Telephone") the debt ratio could be as high as approximately 50 percent.[3] Section VIII(H) further prescribes that the "quality of the debt" of the divested BOCs shall be "representative of the average terms and conditions of the consolidated Bell System debt," but permits exceptions for companies whose current debt "provides a more equitable basis." J.A. 137 n. 321. Second, the District Court required that AT&T's plan for implementing the reorganization be submitted and approved by it, J.A. 172, as well as by the Justice Department. See MFJ, §I(A); J.A. 174.

On August 24, 1982, the District Court, with the parties' consent, entered the MFJ, which contained all the District Court's proposed revisions. On August 26, 1982, the District Court authorized approximately 110 public and private entities and organizations to intervene in this case to appeal the entry of the MFJ, to participate in future District Court proceedings relating to AT&T's plan for implementation of the reorganization, or

[3]During the public interest proceedings, AT&T had shown that Pacific then had a 57% debt ratio because of its adverse local regulatory treatment and financial history and that fairness to AT&T and the other BOCs required that Pacific be divested with a debt ratio of up to approximately 50 percent debt. See, *e.g.*, AT&T Reply Brief, p. 95 n.** (June 24, 1982); see also AT&T Response To Public Comments, pp. 76-77 (May 21, 1982); pp. 23-24, *infra*.

to appeal an order approving that plan. J.A. 191-94. Seventeen intervenors appealed from the entry of the MFJ. On November 10, 1982, the District Court certified these appeals directly to this Court under the Expediting Act, 15 U.S.C. §29(b). This Court summarily affirmed the MFJ on February 28, 1983. *Maryland* v. *United States*, 103 S.Ct. 1240.

**Plan of Reorganization.** On December 16, 1982, AT&T submitted the 471-page Plan of Reorganization ("Plan") that specified the detailed principles and procedures that will govern the division of the Bell System's resources and the implementation of the divestiture under Section I(A) of the MFJ. See J.A. 174-75.[4]

Two provisions of the Plan are directly pertinent to these appeals. First, because the MFJ splits the telephone network at the interexchange switches, MFJ, §I(A)(2), (4), J.A. 174-75, the Plan assigns the BOCs all the investment in telephone plant located on the exchange side of those switches, including all wires, cables, and transmission facilities and excluding only customer premises equipment. Plan, 6-142. Second, the Plan provides that no BOC will be assigned more debt than the MFJ-prescribed debt ratios would allow and that, when necessary to assure compliance with Section VIII(H), AT&T will assume BOC debt. Plan, 191-97. The Plan also then prescribed that each of the companies would be divested with their existing embedded costs of debt. It explained that any attempts to equalize the costs among companies would introduce improper subsidies among regions, "such as low growth areas subsidizing faster growing areas." Plan, 195. At

[4]On October 4, 1982, AT&T and the BOCs had filed the BOCs' proposals for the division of the country into the exchange areas ("LATAs") and associated independent telephone company territories (see MFJ, §IV(G); J.A. 178-79) that will determine which network facilities are exchange facilities to be divested and which are interexchange facilities to be retained by AT&T. After extensive proceedings, these LATAs were, with minor modifications, tentatively approved in an April 20, 1983, Opinion and finally approved in a decision issued on July 8, 1983. J.A. 284-308.

that time, the regional companies had embedded costs of debt of between 8.5% and 9.1%, with the exception of Pacific Telephone which, due to its adverse financial history (see p. 5 n. 3, *supra*), was then at 9.9%. Plan, 194-95. However, more recent data set forth in the Prospectus that the Bell Companies filed with the SEC on November 16, 1983, indicates that, with the exception of Pacific, the debt ratios of the to-be-divested companies will range from 8.79% (Bell Atlantic Corporation) to 9.4% (Southwestern Bell Corporation). See AT&T Information Statement and Prospectus, pp. 63, 83, 105, 127, 151, 174, 195.

**The District Court's Proceedings on AT&T's Plan.** The District Court ordered each of the designated Chief Executive Officers of the seven to-be-divested regional companies ("regional CEOs") to submit sworn statements that addressed whether AT&T's Plan of Reorganization will leave them as financially viable companies with the resources necessary "to perform the functions described in the decree" and whether any provision of the Plan was interposed over their objections. See J.A. 164-65. The seven regional CEOs thus each filed affidavits on December 16, 1983. Only one designated CEO directly questioned the financial viability of his region: Donald E. Guinn of Pacific Telephone who raised objections to the treatment of Pacific Telephone's debt.

In response to Mr. Guinn's objections, AT&T, on April 7, 1983, amended the Plan to provide that Pacific would be divested in a more favorable financial position than is required by the MFJ: an expected debt ratio of less than 47%, not the 50% that the MFJ permits, and an average embedded cost of debt expected to be 9.5%. Mr. Guinn thereupon filed a supplemental sworn statement that withdrew his previous objections. See Second Supplemental Statement of Donald E. Guinn (April 7, 1983). This ended the controversy with Pacific.

Under the procedures that the District Court established, some 50 intervenors and *amici curiae* filed comments and objections to the Plan with the Justice Department and with the District Court.

These pleadings raised literally hundreds of issues and addressed virtually every provision of the Plan.

Section I(A)(1) of the MFJ required the Justice Department to conduct an independent examination of the Plan and to approve or to disapprove it. J.A. 174. Thus, after its initial review of the comments, the Department advised AT&T that over 20 amendments had to be made before it could approve the Plan. AT&T formally made 23 separate amendments to the Plan on March 14, 1983, when it filed its Response to Objections to its Proposed Plan of Reorganization ("AT&T's Response"). After reviewing AT&T's Response, the Department on March 24, 1983, submitted the Response of the United States to Public Comments and Action on AT&T's Proposed Plan of Reorganization ("Response of the United States"). It stated that the Department would not formally approve the Plan unless an additional twelve amendments were made. AT&T agreed to each of these amendments.

Notwithstanding the Department's approval of the Plan, as amended, the District Court called for the submission of additional memoranda from the parties, the seven to-be-divested regional companies, and the intervenors on six separate issues. It conducted a hearing on June 2, 1983, in which it heard live testimony from three of the designated regional CEOs. On July 8, 1983, the court issued a 159-page opinion (J.A. 195-330) which concluded that the amended Plan would not be approved unless it were further modified in six major respects—none of which is relevant to these appeals. J.A. 328-330. California thereafter asked the District Court to reconsider its ruling that complex inside wiring was properly assigned to the BOCs. Contrary to California's misstatement (J.S. 7), the District Court explicitly addressed and rejected California's complex inside wiring claim, see J.A. 339 n. 18, 343-44, as well as the two other claims raised in these appeals. See J.A. 344 ("station handling"); J.A. 221-22 n. 64 (Pacific debt).

AT&T amended the Plan to adopt the District Court modifications, and the court entered an order approving the amended Plan

on August 5, 1983. J.A. 349-50. The State of California and the California Public Utilities Commission ("California") filed a notice of appeal from this decision on August 10, 1983. The New York State Department of Public Services ("New York") filed a notice of appeal on September 13, 1983.

On August 25, 1983, the Justice Department filed a motion urging the District Court to certify California's appeals and any subsequent appeal from the approval of the Plan directly to this Court under the Antitrust Expediting Act, 15 U.S.C. §29(b). AT&T supported this motion. Neither California, New York, nor any other intervenor opposed it. On September 7, 1983, the District Court issued the certificate, finding that the same basic considerations that dictated direct Supreme Court review of the entry of the MFJ are "equally applicable" here. J.A. 351-54.

## REASONS FOR SUMMARY AFFIRMANCE

By directly reviewing the entry of the MFJ last February, this Court recognized that this case has such profound importance for the national economy that it epitomizes the government antitrust actions in which Congress intended direct Supreme Court review of a District Court's final decision. Because a failure to resolve the legal challenges to this reorganization before it occurs on January 1, 1984, would threaten the very success of this massive effort, the considerations that led the Court to review the entry of the MFJ have even greater force now, only weeks before divestiture. These appeals, moreover, present claims that are far less substantial than those as to which the Court affirmed summarily last February. The decision below should be summarily affirmed.

### I. EXPEDITION OF THESE APPEALS UNDER THE EXPEDITING ACT IS A MATTER OF PARAMOUNT PUBLIC IMPORTANCE.

In the Antitrust Expediting Act, 32 Stat. 823, *as amended*, 15 U.S.C. §29(b), Congress found that public antitrust cases can have an enormous "impact on the economic welfare of this nation," that they "are unlike other federal cases," and that it is often

necessary and appropriate to expedite the final decision in such cases by making final judgments directly appealable to this Court. H.R. Rep. No. 93-1463, 93d Cong., 2d Sess. 14 (1974); see S. Rep. No. 93-298, 93d Cong., 1st Sess. 3-4 (1973). Although Congress has eliminated the previous requirement that there be direct Supreme Court review in all Government antitrust cases, see 15 U.S.C. §29(a),[5] it retained direct appeals for those Government antitrust cases in which "the district judge who adjudicated the case enters an order stating that immediate consideration of the appeal by the Supreme Court is of general public importance in the administration of justice." 15 U.S.C. §29(b). In such cases, the Act provides that this Court may then either "dispose of the appeal . . . in the same manner as any other direct appeal" or remand it to the appropriate court of appeals, where it will be subject to the ordinary appellate procedures. *Id.*[6]

These appeals present precisely the kind of cases that Congress intended to preserve for direct Supreme Court review. By summarily affirming the entry of the MFJ, this Court recognized that any significant delays in the final resolution of the legal challenges

[5]Congress wished to relieve the Court of the burden of reviewing voluminous records. See S. Rep. No. 93-298, *supra*, p. 8. That is not a consideration here because the question presented is the purely legal question of whether the parties who drafted the MFJ and the District Judge who entered it have misinterpreted it and, even if they have, whether the order approving the Plan represents an abuse of the District Court's discretion.

[6]The Expediting Act, however, was not intended to "bestow on the Supreme Court an unqualified discretion to hear or not hear a case." H.R. Rep. No. 93-1463, *supra*, pp. 13-14 (1974). On the contrary, Congress "intended that the Supreme Court hear cases that are of general public importance in the administration of the antitrust laws." *Id.* The standard for direct appeals is *not* that the case raises novel or unsettled legal issues or is otherwise immediately review-worthy under 28 U.S.C. §1254(1) (Supreme Court review prior to judgment in the Court of Appeals). *Id.* As the District Court stated in its opinion certifying these appeals directly to this Court: "Even though it is not likely that the appeals will present questions of legal significance, they are clearly of general public importance." J.A. 352 (footnote omitted).

to the reorganization of the Bell System create uncertainty that threatens the interests of the Nation. See J.A. 148-49. As the District Court found, the uncertainty that the instant appeals create threatens the same serious adverse consequences; if anything, expedition is even more necessary now because the "January 1 deadline" is only six weeks away and the adverse consequences of continued uncertainty "would be multiplied if the divestiture proceeded on January 1, 1984, while the plan of reorganization was still under challenge in the courts." J.A. 353.

California (J.S. 8-9) and New York (J.S. 8) argue that their appeals raise issues that are discrete and unrelated to other aspects of the reorganization and that delay in the final resolution of their appeals for months or even years after divestiture will have no adverse consequences. As is more fully explained in AT&T's Motion For Expedition Of These Appeals, this is simply incorrect. These challenges implicate the heart of the reorganization. If a decision were issued after divestiture that required a reassignment of complex inside wire, for example, it would disrupt operations, business planning, customer relationships and regulatory decisionmaking and would require post-divestiture reassignments of employees and possible reallocation of BOC debt. Similarly, if California were to prevail on its claim that Pacific's average cost of debt is too high, the embedded debt of the BOCs would have to be pooled and reallocated among the BOCs. Finally, a reversal on any of the grounds raised could also lead the parties to reconsider these and other provisions of the MFJ and Plan, because any significant change in the Plan could destroy the careful balance the MFJ was intended to achieve. The pendency of the appeals, accordingly, creates uncertainty that precludes reliable valuation of any of the to-be-separated companies, impairs access to capital markets, impedes operational decisions, threatens massive post-divestiture disruptions, and prolongs the very interrelationship among Bell System companies that entry and affirmance of the MFJ were supposed to end.

## II. THE APPEALS HAVE NO SUBSTANCE AND SHOULD BE SUMMARILY AFFIRMED.

California's and New York's appeals are each frivolous, and the District Court's order approving the Plan of Reorganization should therefore be summarily affirmed. Appellants contend that the three provisions of the Plan—relating to "complex" inside wiring, accounting entries for "station handling", and the average cost of Pacific Telephone's long term debt—violate the MFJ. These contentions are insubstantial on their face. As an antitrust consent decree, the MFJ "is to be construed for enforcement purposes basically as a contract" between the parties to the case, *United States* v. *ITT Continental Baking Co.* 420 U.S. 223, 238 (1975); see *United States* v. *Armour & Co.*, 402 U.S. 673 (1970).

The decisive consideration here is that the challenged provisions of the Plan were drafted to implement the MFJ by one party to the case (AT&T), reviewed and agreed to by the other party (the United States), and were approved as consistent with the MFJ by the District Court following extensive public proceedings. Appellants' contentions thus reduce the untenable claim that an antitrust consent decree can be misinterpreted both by the parties who negotiated it and agreed to it and by the District Judge who entered it after conducting proceedings going beyond those prescribed by the Tunney Act.[7]

Moreover, even if there were a basis for appellants' claim that MFJ has somehow been modified, *sub silentio*, the District Court's decision is reviewable, *at most*,[8] for abuse of discretion.

[7]Because a principal purpose of that Act is to eliminate subsequent disputes over the meaning of antitrust consent decrees, see H.R.Rep. No. 93-1463, 93d Cong. 2d Sess. 8 (1973), the fact that the District Court upheld the interpretations of the parties who drafted and negotiated the MFJ should be conclusive.

[8]This Court has held that where, as here, there is no claim of fraud, lack of jurisdiction, or mistake, a judicial order "rendered by consent [of the parties] is always affirmed without considering the merits of the case." *Swift & Co.* v. *United States*, 276 U.S. 311, 323-24 (1928) (Sherman Act); *accord*, *NLRB* v. *Ochoa Fertilizer Corp.*, 368 U.S. 318, 323 (1961).

See, *e.g.*, *Patterson* v. *Newspaper & Mail Deliverers Union*, 514 F.2d 767, 771-72 (2d Cir. 1975) *cert. denied*, 427 U.S. 911 (1976); *Metropolitan Housing Development Corp.* v. *Village of Arlington Heights*, 616 F.2d 1006, 1015 (7th Cir. 1980). Because the challenged provisions of the Plan promote the Justice Department's antitrust objectives and are manifestly reasonable, neither appellant even claims, much less establishes, that the District Court's discretion was abused.

Appellants' claims, accordingly, can be rejected without even considering the merits of their arguments. However, a detailed examination of their contentions even more vividly demonstrates that there is no basis whatever for holding that the District Court's approval of the Plan was improper.

### A. The Plan Properly Assigned The Investment In "Complex" Inside Wiring And "Station Handling" To The BOCs.

California and New York challenge the Plan's assignment to the BOCs of investment in portions of one of the BOCs' accounts, Account 232—Station Connections. California challenges the assignment of "complex" inside wiring and—contrary to its position in the District Court—of all "station handling" costs. In contrast, New York confines its challenge to the treatment of "station handling." Neither claim has any merit.

All of the investment in Account 232 has been incurred for only one purpose: to extend local transmission facilities and connect them to newly installed telephone handsets located on customers' premises. The investment in Account 232 includes the wire that runs from outside the customer's premises through his walls to the standard telephone jack ("simple inside wire"), the wire that runs through walls and floors of skyscrapers and other buildings to connect private switchboards with jacks for the individual telephone handsets ("complex inside wire"), the jacks themselves, and other physical assets. Account 232 "investment" also includes the accounting entries that have been made when tele-

phone company service personnel visit customers' premises to install this wiring, test it, and connect it to handsets or private switchboards. These are "capitalized" labor costs.

The assignment of the entire Account 232 investment to the BOCs follows from the terms and purpose of the MFJ. By its terms, the MFJ splits the telephone network at the point of interexchange switching and provides that all investment on the exchange side of those switches be assigned to the BOCs, with the sole exception of customer premises equipment. MFJ, §§I(A)(2), (4); J.A. 174-75. This is because one of the basic purposes of the MFJ is to separate ownership of the Bell System's interexchange facilities and CPE from its local transmission and switching facilities and thereby to assure that AT&T does not control both an embedded CPE business and "bottleneck" facilities to which all CPE vendors must have access.

Accordingly, in the District Court, both the Justice Department and the trade association of customer premises equipment competitors of AT&T vigorously argued that the facilities in Account 232 must be assigned to the BOCs. Specifically, each argued that the assignment of either "complex" or "simple" inside wire to AT&T would give it control over a facility essential to the CPE business and give it the very opportunity to deny access to CPE competitors that the MFJ was intended to end. See Response of United States, pp. 87-90; Comments of North American Telephone Association, pp. 21-22; *accord,* Kansas Public Service Commission Comments, p. 2.[9] The District Court agreed. It found that both simple and complex inside wire is part of the local

[9]The Department's and the CPE vendors' position flatly refutes California's argument (J.S. 15) that the assignment of inside wire to the BOCs will permit AT&T to "reap excessive profits" or "undercut its competitors" in the CPE market. Whether or not AT&T has a sunk investment for complex inside wiring on its books is irrelevant to its competitive posture. The price AT&T can charge for CPE is dictated by competition. If AT&T tried to charge more than a competitive price for its CPE, customers would turn to other vendors.

exchange "bottleneck" and that assignment of it to AT&T would "insert AT&T-controlled facilities between the Operating Companies and the subscribers, and . . . thus be entirely inconsistent with the basic purposes of the decree." J.A.344. Even if the terms of the MFJ were not so clear, these findings preclude any claim that the District Court abused its discretion in approving this provision of the Plan.

**Complex Inside Wire.** California acknowledges that the Plan properly assigned "simple" inside wiring to the BOCs. However, of the 110 intervenors in this case, California alone now contends that "complex" inside wiring is somehow different and should have been assigned to AT&T, not the BOCs. It accuses the District Court of having "failed to address" California's contention. (J.S. 7) This is false. The court explicitly held, in ruling on California's own request for reconsideration, that complex inside wiring is part of the "local exchange bottleneck" and that California's position is therefore "entirely inconsistent with the basic purpose of the Decree." J.A.344.

California's arguments boil down to an attempt to rewrite the MFJ. California recognizes that the parties unequivocally intended to assign all inside wiring to the BOCs and that inside wiring was therefore excluded from the MFJ's definition of CPE.[10] Nonetheless, California now makes (J.S. 14-15) two arguments under which complex inside wiring would become CPE. First, California argues that complex inside wire is "equipment employed . . . to route telephone calls" and thus satisfies the MFJ's definition of CPE. MFJ, §IV(E); J.A. 177. But wire transmits

[10]California acknowledges that the parties implemented their intention by incorporating the definition of CPE from the FCC's decision in the *Second Computer Inquiry*, 84 F.C.C.2d 50, 61 n. 10 (1980)—a definition that expressly excludes inside wiring. This definition fixes the meaning of MFJ. The fact that the FCC may hereafter change its definition of CPE, under the different standard of the Communications Act of 1934 (see California J.S. 17 n. 18), is irrelevant to the meaning of the MFJ.

calls; it does not "route" them. This part of the definition of CPE refers only to switching equipment, not to wire. See, *e.g.*, Response of United States, p. 88.

California also argues that complex inside wire should be assigned to AT&T on the theory that it "relates to" CPE within the meaning of Section I(A)(2) of the MFJ. J.A. 174. But, again, the parties have made it explicit that assets "relating to" CPE are confined to those necessary for its installation, sale, or delivery, such as trucks or phone stores. See, *e.g.*, Response of the United States, p. 87, n.*; AT&T's Response, p. 157 n.*. More fundamentally, California's two textual arguments are flatly inconsistent with its proposed distinction between "complex" and "simple" inside wiring and would vitiate the whole MFJ. If complex inside wiring "routes" calls or "relates" to CPE, then so do simple inside wiring, telephone jacks, and even the wire that runs from outside customers' premises through streets and alleys to the BOCs' central offices—all of which epitomize the "bottleneck" facilities that are to be divested and structurally separated from AT&T's CPE business.

**Station Handling.** In contrast to California, New York acknowledges that the BOCs were properly assigned both the complex and simple inside wiring. However, New York objects to the treatment of a different aspect of Account 232: a portion of the accounting entries that reflect telephone servicemen's "capitalized labor." New York concedes that the major portion of this capitalized labor "investment" represents the servicemen's installation and testing of inside wiring and was properly assigned to the BOCs. However, New York notes that servicemen also perform the function of connecting the inside wire to telephone handsets—known as "station handling"—and New York insists that some portion of the capitalized labor in Account 232 should now be allocated to station handling and assigned to AT&T. Ironically, although California now makes the same argument, it express-

ly disclaimed New York's position in the District Court because of the severe adverse effect it would have on the economic balance that the MFJ was designed to preserve. See also J.A. 339 n. 18.[11]

There is no merit to New York's and California's current claim. Station handling represents the capitalization of labor costs incurred in connecting local transmission facilities to telephone desksets. There is no principled basis for distinguishing this function from any other function whose cost is recorded in Account 232. Station handling is simply the last act in establishing a working station connection.

Furthermore, there is no way to determine what portion of the "capitalized labor" in Account 232 represents time spent in connecting a customer's telephone instrument to local transmission facilities and what portion the time spent testing and installing inside wire or telephone jacks. Telephone company service personnel simply have had no reason or occasion to make an artificial distinction between these interrelated functions and have made no record of the time spent on the respective tasks because the FCC's accounting rules have never made any such distinction. See 47 C.F.R. §31.232. Contrary to appellants' arguments, there is no way to segregate station handling costs from all other costs in Account 232—other than sheer guesswork. The appellants' own arguments vividly demonstrate that any attempt by the District Court to make such "estimates" would introduce into the asset assignment process precisely the valuation proceedings and

[11]In the District Court, California urged only that there be a distinction between complex and simple inside wiring. Because California recognized that the assignment of simple inside wiring and associated station handling "investment" to AT&T would present "special cost recovery problems" for the Bell System's three million shareholders, see California's Further Comments On The Plan Of Reorganization, pp. 20-21 (February 11, 1983), California confined its claim to complex inside wiring. See also California's Reply Comments on the Plan of Reorganization, pp. 25-26 (April 12, 1983) (complex inside wiring "is distinguishable from other elements of Account 232, and so should be transferred to AT&T").

unauditable uncertainty that the MFJ was carefully drafted to avoid.[12] See J.A. 124-33. For these reasons, the District Court found that "there is no practical way to separate out" this part of the capitalized labor entries. This holding implemented the terms and purposes of the MFJ and, in any event, was a sound exercise of discretion.

The appellants' further arguments are meritless. First, New York's argument (J.S.7) that a failure to assign station handling investment to AT&T is anticompetitive rests on a misunderstanding of these accounting entries.

Station handling "investment" is not a physical asset. It is an accounting entry to reflect the fact that, prior to 1981, all the labor costs imputed to the installation of wiring and telephone instruments were not recovered at the time of their installation, but instead were capitalized and recovered through depreciation charges over many years. This occurred pursuant to regulatory policies designed to keep the price of establishing new telephone service artificially low. Beginning on January 1, 1981, the FCC ordered companies to begin recovering all such costs at the time each installation is made, which, under accounting principles, means that the labor costs are "expensed."[13] Because the FCC has ordered that the investment in Account 232 on January 1, 1981, be amortized over 10 years, the Bell System's shareholders' recovery of this pre-1981 investment is nearly 30% complete; the

[12]New York's estimates of the BOCs' station handling "investment" in New York alone vary by a factor of six—from $106 million to $600 million. J.A. 7. New York's suggestion (J.S. 6) that this extraordinary margin of guesswork is typical of the uncertainty in dividing other assets pursuant to the MFJ is wrong. In every other provision of the Plan, whole accounts or subaccounts are assigned, or accounts (*e.g.*, for land and buildings) are divided because records exist that permit the assets to be accurately separated and assigned.

[13]*Amendment of Part 31 (Uniform System of Accounts)*, 85 F.C.C. 2d 818, 819, 823-29 (1981). The FCC gave state regulatory commissions the option of requiring the expensing of all these costs after January 1, 1981, or of phasing in expensing over a four year period.

issue here pertains only to the amounts now in Account 232: *i.e.*, approximately 70% of the capitalized labor costs incurred before 1981.

These accounting entries and regulatory recovery principles are simply irrelevant to post-divestiture competition.[14] For example, there are instances in which two telephones were manufactured in 1980 and are identical in all respects, except one was installed by a BOC in 1980 (with capitalized labor of $60 recorded in Account 232) and the other was installed by a BOC in 1981 (and no entry made in Account 232). Both telephones will be assigned to AT&T on January 1, 1984. Because the two telephones are identical, they will be offered at the same price, and the price that AT&T will be able to charge cannot exceed competitors' prices in the intensely competitive CPE market. It is absolutely irrelevant to AT&T's price—as well as to prices of AT&T's competitors—whether AT&T is also assigned the entire sunk "investment" in Account 232 for the telephone installed in 1980. It is equally irrelevant to post-divestiture competition whether AT&T is assigned that portion of the total "capitalized labor" in Account 232 that may be estimated to represent "station handling."[15]

Second, appellants argue that assigning the disputed parts of Account 232 to the BOCs will unfairly burden regulated rate-

[14]California's related argument that the Plan's assignment of station handling to the BOCs permits AT&T to obtain CPE at less than its full cost is even more fundamentally erroneous. First, it ignores that the reorganization of the Bell System is not a sale of assets, but a split of a single enterprise's assets in which purchase and sale concepts have no place—as the District Court explicitly found when it rejected one of California's earlier claims. J.A. 125-30. Second, the assets will be transferred onto AT&T's books of account at their historical "book" value, which the District Court found to be the correct valuation and cost standard for the transfers. J.A. 130-33.

[15]California's own regulatory practice confirms the irrelevance of sunk station handling costs to competitive CPE pricing. As California acknowledges (J.S. 12 n. 13), no portion of the station handling costs recorded in Account 232 is included in the prices at which it has authorized Pacific to sell CPE to telephone subscribers.

payers. This argument not only rests on a misunderstanding of these accounting entries, but also demonstrates why the District Court held that an assignment of all of Account 232 to AT&T would destroy the careful economic balance that the MFJ sought to preserve and needlessly destroy the investments made by the Bell System's three million shareholders. J.A. 339 n.18; see also *id.* at 323-28.

The reason that there are entries in Account 232 today is that regulatory commissions did not permit labor and other costs to be expensed and recovered at the time telephone installations were made—as they would have been in an unregulated business—until January 1, 1981. Although the Bell System's shareholders have recovered their costs for installations made after January 1, 1981, they have had a severe cost-recovery problem relating to the Account 232 investment that is on the BOCs' books and that pertains to the period before January 1, 1981. The FCC has adopted an equitable solution. It requires local exchange carriers, like the BOCs, to recover the Account 232 investment over a ten year period. The BOCs have been permitted to make this recovery, in large measure, from local ratepayers.[16] This reflects two facts. First, this sunk investment cannot be recovered by inflating CPE prices because of the intensely competitive markets for CPE that the FCC has created.[17] Second, it is the fairest mode of recovery because general ratepayers, as a class, benefitted from the expansion of telephone service that the previous artificially low installation charges made possible.

The effect of California's and New York's proposal would be to interrupt the process of cost recovery (now 30 percent completed)

[16]The BOCs are also free to recover these sunk investments from current users of inside wire. Under the Plan, this source of revenues will continue to be available to the BOCs.

[17]For example, AT&T could not recover the entire investment from the current users of inside wire or CPE customers because the total investment built up over years far exceeds the costs associated with current customers' use.

in midstream and renege on the regulatory obligation to permit the Bell System's three million shareholders to recover their capital. For these reasons, the assignment of the disputed portions of Account 232 to AT&T would upset the careful economic balance that the MFJ was designed to preserve, J.A. 339 n. 18—as well as violate its explicit terms and competitive objectives.

### B. The Plan Provides For The Divestiture Of Pacific Telephone In A More Favorable Financial Condition Than The MFJ Requires.

California also objects to the Plan's provision that Pacific Telephone will be divested with a higher average cost of debt than the other BOCs. This claim is not only contrary to the plain terms and purposes of the MFJ, but ignores the reality that the amended Plan will leave Pacific in a far more favorable financial position than is required by even California's own construction of the MFJ.

Under the amended Plan, Pacific will be divested with a debt ratio of approximately 46.5%, which is substantially less than the approximately 50% debt ratio that Section VIII(H) of the MFJ permits, and an average cost of funded debt of approximately 9.5%. California's position is that the average cost of Pacific's debt must be reduced to 9.2% (J.S. 20 n.20). California reasons that this further reduction must occur before Pacific's debt will be of a "quality . . . representative of the average terms and conditions" of the Bell System's debt. See MFJ, §VIII(H), J.A. 184-85.

California's claims are meritless. Section VIII(H) does not require equalization of debt costs between Pacific and the other BOCs. In prescribing a higher debt ratio for Pacific than for the other BOCs, Section VIII(H) expressly recognizes that Pacific cannot be placed on an equal footing with the other companies. Pacific's average cost of debt is higher than the other BOCs for the same reason that the MFJ permits it to be divested with more debt: its adverse financial history and regulatory treatment by California (see p. 5 n. 3, *supra*; pp. 23-24, *infra*). The District

Court could not have authorized disparate treatment of Pacific in one clause of Section VIII(H) and then required complete equality in a second. See AT&T Response, 277-278.

But even if the first sentence of Section VIII(H) required the equalization of debt costs, the second sentence of the section —which California ignores—provides that "the Court may grant an exception to this requirement." J.A. 185. An exception is appropriate if it "can be shown that, with respect to a particular Operating Company, its own current debt provides a more equitable basis." J.A. 137 n. 321. Before the District Court, both AT&T and the United States took the position that if an exception was required to permit Pacific to be divested with its own cost of debt, the District Court should grant that exception in view of Pacific's unique financial and regulatory history.[18] In approving the Plan, the District Court unequivocally rejected California's claim that the MFJ requires a further reduction in Pacific's average cost of debt. J.A. 221-22 n. 64.

The District Court gave four separate reasons for rejecting California's position. Each is unassailable. First, the District Court found that any attempt to equalize Pacific's and the other BOCs' debt costs would require ratepayers in regions of the country that have experienced slow growth to subsidize telephone service for ratepayers in regions that have experienced high growth and in which the local telephone companies have had to borrow more often and more recently.[19] J.A. 221-22 n. 64. The subsidy California seeks would give Pacific lower debt costs than Southwestern Bell (9.4%), as to whose debt there is no dispute, and thus—perversely—would treat Pacific more favorably than

[18]See AT&T's Response, p. 298; Response Of United States, pp. 119, 122.

[19]California is in error when it asserts (J.S. 19) that equalizing the BOCs' cost of debt would not affect the other BOCs' finances or require substantial transfers among companies. Illinois Bell and Northwestern Bell, for example, would have their annual debt costs increased by approximately $10 million and $13 million in the first year alone; and overall, four of the seven regional companies would be net payers to the other three regions. See AT&T's Response, p. 279. The Staff of the Federal

another "Sun-belt" company that was not afflicted with the same history of unreasonable regulation and financial difficulty. Indeed, contrary to California's position, Pacific's chairman agreed to the divestiture of his company with a debt cost of 9.5% precisely because such costs were "in line with the other high growth 'Sun-belt' Bell Operating Companies." Second Supplemental Statement of Donald E. Guinn, p. 1 (April 7, 1983). As the District Court held, to further subsidize Pacific's debt costs in these circumstances would be manifestly unfair.

Second, the District Court found that such subsidies would lead to "new and continuing AT&T entanglements with the Operating Companies." J.A. 221-22 n. 64. The District Court correctly held that this would preserve the very financial integration of the Bell System that the MFJ was intended to end. *Id.*

Third, the District Court found that Pacific's adverse financial condition before divestiture was "due in large part to the action of California's regulators" (J.A. 137) and that "Pacific will be divested in as financially sound a condition as its prior history permits." J.A. 221-22 n. 64.[20] Contrary to California's arguments, the record demonstrates that, for more than a decade, the California commission steadily depressed Pacific's earning to levels that did not attract needed equity capital and that Pacific, consequently, was forced to rely increasingly on debt financing, which raised its cost of debt and raised its debt ratio from 48.6% in 1973 to 59.1% in 1980. This led to steady deterioration of

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Communications Commission agrees. It found that to divest Pacific Telephone with the Bell System's average cost of debt "would amount to a subsidy to [Pacific] and California consumers directly by other segments of the Bell System and indirectly by other Bell System customers." FCC Staff Analysis of AT&T Reorganization Plan, pp. 27-28 (February 11, 1983).

[20] *Accord*, FCC Staff Analysis of AT&T Reorganization Plan, pp. 27-28 (February 11, 1983) ("[Pacific's] debt ratio and cost of debt may be considered indicative of the condition of utilities in California . . . [Pacific's] financial difficulties, then, may simply reflect the risks a utility faces in California.").

Pacific's debt rating (from AAA in 1973 to A– in 1980).[21] See Sworn Statement of Donald E. Guinn, p. 9 (filed December 16, 1982). The MFJ manifestly was not intended to restore Pacific to the same balance sheet condition as those BOCs who have been subjected to less onerous regulatory treatment. To the contrary, Section VIII(H) recognizes that Pacific's debt situation differs from that of the other BOCs.

Finally, the District Court found that the Plan would, if anything, produce an impressive improvement in Pacific's financial condition, far in excess of that enjoyed by any other BOC. J.A. 221-22 n. 64.[22] Indeed, Pacific will be divested in a better financial position than is required by any interpretation of the MFJ, including California's. The following table, setting forth Pacific's total annual debt expense under four assumptions, illustrates this point.

**Pacific Telephone's Debt Expense**

| Assumption | Debt Ratio | Total Debt (billions) | Cost of Debt | Annual Debt Expense (millions) |
|---|---|---|---|---|
| 1. MFJ As Construed By Parties..... | 50.0% | $6.104 | 9.7% | $592 |
| 2. MFJ As Construed by California ..... | 50.0% | $6.104 | 9.2% | $562 |
| 3. Plan of Reorganization | 46.5% | $5.676 | 9.5% | $540 |
| 4. California Proposal in this Court..... | 46.5% | $5.676 | 9.2% | $522 |

[21]During those years, the securities rating firms were unanimous in their view that the principal cause of Pacific's decline was unreasonable state regulation. See Duff & Phelps, Inc., "Review of Pacific Telephone," p. 1 (November 29, 1980) ("We would rank the California regulatory climate as about the worst among any that regulate the Bell System."); Standard & Poor's, *Fixed Income Investor*, p. 171 (October 22, 1977) ("regulatory treatment in California has been consistently below average for Pacific Telephone"). See also Moody's, *Bond Survey*, p. 524 (November 12, 1979).

[22]On March 28, 1983, Standard & Poor's, a securities rating firm, raised Pacific's debt rating from A– to A+, citing "the singular advantages that the company is expected to realize from divestiture." Standard & Poor's, *Credit Week*, p. 1942. Pacific was the only Bell System company to have its debt rating raised. *Id.*

Under the parties' construction of the MFJ (Assumption 1) Pacific could have been divested with 50 percent debt and its own cost of debt (9.7%), resulting in annual debt expenses of $592 million. Under California's construction of the MFJ (Assumption 2), Pacific could again have 50 percent debt, but with an average cost of debt of 9.2%, resulting in annual expenses of $562 million. However, Pacific's annual debt expenses under the Plan of Reorganization as approved by the District Court in the order appealed from (Assumption 3) will be only $540 million, some $22 million less than under California's own construction of the MFJ.[23] Under the proposal in California's Brief (p. 20 n.20), Pacific's debt expense would be lower still—$522 million (Assumption 4), but California assumes that it could insist on its reading of the debt cost provisions of the MFJ and also retain for Pacific a lower debt ratio than it acknowledges is provided by the MFJ. J.S. 19.

California cannot have it both ways. In the event the MFJ were construed to require that Pacific be divested with less than its own cost of debt, AT&T would withdraw that portion of the Plan providing Pacific a debt ratio lower than that required by the MFJ. In any event, however, because the Plan will result in a substantial improvement in Pacific's financial condition and leave Pacific better off than is required by any interpretation of the MFJ, it is apparent that California has neither legal nor practical grounds to complain that the Plan departs from the MFJ.

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[23]California acknowledges that the MFJ does not require Pacific to be divested with exactly the System average cost of debt (approximately 8.8%), which would treat it more favorably than several other BOCs. But even if Pacific were given debt costs of 8.8%, its annual debt expense (with the MFJ-prescribed debt ratio of 50%) would remain $540 million, leaving Pacific no better off than it will be divested under the Plan.

## CONCLUSION

The District Court has shown that a trial court can expeditiously manage big antitrust cases and assure that the uncertainty that they create does not imperil vital national industries. The expedition of this appeal under the procedures Congress has established will enable the judicial system to continue to protect these public interests.

For the reasons stated, the appeals in this case should be decided by this Court before January 1, 1984. They are so lacking in merit that they should be affirmed summarily. This will remove the uncertainty that threatens the national telecommunications network while the Bell System completes the largest corporate reorganization in our nation's history.

Respectfully submitted,

HOWARD J. TRIENENS*
ALFRED A. GREEN
JIM G. KILPATRIC
FRANCINE J. BERRY
195 Broadway
New York, New York 10007
(212) 393-5111

GEORGE L. SAUNDERS, JR.
JOHN D. ZEGLIS
DAVID W. CARPENTER
DAVID D. HILLER
One First National Plaza
Chicago, Illinois 60603
(312) 853-7000

*Of Counsel:*
SIDLEY & AUSTIN

November 22, 1983

*Counsel of Record

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Nos. 83-737 and 83-738

IN THE SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1983

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THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, Appellants,

v.

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY AND AMERICAN TELEPHONE and TELEGRAPH COMPANY, Appellees.

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NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE, Appellant,

v.

UNITED STATES OF AMERICA and WESTERN ELECTRIC COMPANY AND AMERICAN TELEPHONE and TELEGRAPH COMPANY, Appellees.

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On Appeal From the United States District Court for the District of Columbia

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# AT&T'S MOTION TO EXPEDITE THESE APPEALS

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Appellees Western Electric Company and American Telephone and Telegraph Company ("AT&T"), by their attorneys, hereby move for expedition of these appeals. These two appeals represent the final legal challenges to the structural reorganization of the Bell System which was ordered in the District Court's Modification of Final Judgment ("MFJ") on August 24, 1982, and which will occur in less than six weeks, on January 1, 1984. Seventeen appeals were filed from the entry of MFJ, taken directly to this Court under the Antitrust Expediting Act, 15 U.S.C. §29(b), and decided by this Court on an expedited basis last term. Maryland v.

United States, 103 S. Ct. 1240 (Feb. 28, 1983). The instant appeals, in turn, are challenges to the District Court's decision approving AT&T's and the Justice Department's plans for implementating the MFJ, and these appeals, too, have been certified directly to this Court. The District Court found that it is a matter of profound "public importance in the administration of justice" that the final disposition of these challenges occur before January 1, 1984. J.A. 353; see November 10, 1982 Order, p. 3. Accordingly, AT&T moves for the consideration of its motion for summary affirmance at the next scheduled conference of the Court and for a decision before January 1, 1984. In support of this motion, AT&T states as follows:

1. The MFJ achieves the Justice Department's antitrust objectives in over three decades of litigation with the Bell System. It orders the divestiture of the Bell System's local exchange functions, which will represent about $100 billion of its approximately $150 billion in assets. The MFJ is to be implemented on January 1, 1984, by dividing the present Bell System into nine separately owned entities (AT&T, seven regional companies, and the region-owned Central Staff Organization). It requires a separation of assets and personnel of each of the major components of the Bell System: AT&T, the 22 Bell Operating Companies ("BOCs"), Western Electric Company, and Bell Telephone Laboratories.

2. The planning to implement the MFJ has been an enormous and unprecedented undertaking. It has been accomplished while the Bell System has continued to provide telecommunications services that are vital to the national economy and the national defense. This split must be completed as of January 1, 1984, and as more fully explained below, if any and all legal challenges to this reorganization are not resolved before that date, this massive effort and important national interests will be jeopardized.

3. When seventeen intervenors appealed the decision entering the MFJ, the District Court found that the existence of legal challenges to the reorganization, no matter how insubstantial, created uncertainty that imperiled vital national interests. It concluded that any significant delays in the final resolution of this case would disrupt the Bell System companies "own operations," "inhibit investment and other business decisions necessary to the maintenance and improvement of the telecommunications network," "jeopardize the ability of the Bell System's components to raise the outside capital needed for the modernization and expansion of [the] network," and "adversely affect the entire telecommunications industry and thus, indirectly, the nation as a whole." J.A. 148-149; see also April 8, 1982 Order, pp. 5-6; November 10, 1982 Order. The District Court specifically found that if the challenges were not finally resolved before January 1, 1984, it would have even more severe consequences. November 10, 1982 Order, p. 3. Accordingly, the appeals were certified directly to this

Court under the Antitrust Expediting Act, id., and this Court decided the appeals on an expedited basis during the 1982 term. See Maryland v. United States, 103 S. Ct. 1240 (Feb. 28, 1982).

4. During the fifteen months since the MFJ was entered, the parties, the District Court, and more than 50 intervenors have invested great resources in assuring that it may be implemented, as scheduled, on January 1, 1984. First, the BOCs, in consultation with the Justice Department, divided the Nation into the exchange areas (" LATAs") and associated nonBell territories that are a precondition to the division of assets. After extensive proceedings that addressed both the geographic boundaries and a host of related issues, the LATAs were approved, with minor modifications. Second, AT&T, in consultation with the BOCs and the Justice Department, prepared the 471-page Plan of Reorganization ("Plan") that is at issue in these appeals and submitted it to the District Court on December 16, 1982 -- over a year before the scheduled reorganization. The Plan was then subject to a separate proceeding that included the filing of sworn affidavits by the designated Chief Executive Officers of the seven to-be-divested regional holding companies on the adequacy of the Plan, the filing of extensive public comments objecting to specific provisions, careful review of the public comments and formal statements of approval and disapproval by the Justice Department, a hearing featuring legal arguments and live testimony by three of the designated regional Chief Executive Officers, and ultimate review by the District Court.

5. In recognition of the overwhelming need to put a timely end to any and all uncertainty over how the MFJ was to be implemented, AT&T took extraordinary steps to avoid any continuing controversies over its plan. It amended the Plan on April 7, 1983, to eliminate Pacific Telephone's objections to its capital structure and to assure that Pacific will be divested in a more favorable financial condition than the MFJ requires. AT&T further agreed to each of the some thirty-five amendments that the Justice Department insisted be made to the Plan. Finally, AT&T acquiesced in each of the six additional major modifications that the District Court required. J.A. 328-330. This was despite the fact that many of the amendments had severe adverse consequences for AT&T and, in its view, were not required by the MFJ: e.g. the District Court's holding that the MFJ denied AT&T any domestic rights to the "Bell" name and trademark. J.A. 329.

6. When, on August 10, 1983, the State of California and the California Public Utilities Commission ("California") appealed from the District Court's decision approving AT&T's plan, as amended, the Justice Department urged, and the District Court found, that the same basic considerations that had led to the expedition of the challenges to the entry of the MFJ last year now dictated the "immediate consideration by the Supreme Court" of any and all appeals from the approval of the plan for the MFJ's implementation. J.A. 354. The District Court reiterated its earlier findings that the uncertainty that challenges to the reorganization

create has "serious adverse consequences" for "millions of [Bell System] employees and shareholders, the Nation's telephone subscribers, AT&T's competitors, the telecommunications industry in general, and the responsibilities of federal and state regulatory bodies." J.A. 353. The District Court found that the pendency of these appeals would have these adverse consequences despite the fact that "it is not likely that the appeals will present questions of legal significance." J.A. 352. Indeed, the Department argued and the District Court found that expedition is even more necessary now than it was when the MFJ was entered because the "January 1 deadline" was "four months rather than almost fourteen months away" and the adverse social and economic consequences of uncertainty "would be multiplied if the divestiture proceeded on January 1, 1984, while the plan of reorganization was still under challenge in the courts." J.A. 353. Thus, the District Court certified these appeals to this Court to permit it to eliminate these threats to the national economy in the only way possible: decision of these appeals before January 1, 1984.

7. In their jurisdictional statements filed November 3, 1983, California and the New York State Department of Public Service ("New York") each implicitly recognize the paramount importance of expedition in this case. However, they argue that the issues that they have raised are discrete and unrelated to the implementation of the MFJ and that there can be no adverse consequences to the public if divestiture proceeds on January 1, 1984, without a prior

final resolution of their claims. This is wrong. The pendency of these appeals would then produce a continuation of the very "state of limbo" that the District Court, the Justice Department, and this Court's decision of last February all sought to prevent.

8. New York and California are simply incorrect in asserting that the assets, liabilities and books of account that are relevant to their appeals can be reassigned between the BOCs and AT&T after the January 1, 1984, divestiture without imperiling the reorganization and the private and public interests that are at stake.

A. For example, California objects to the assignment to the BOCs of the "complex inside wire" -- which is the wire that runs through floors and walls of skyscrapers and other buildings and that performs local transmission functions for business telephone systems such as Private Branch Exchanges ("PBXs"). A post-divestiture reassignment of this physical asset from the BOCs to AT&T would severely disrupt each of the companies' marketing and financial operations, customer relationships, and employee morale during the critical period in which the separate companies must establish separate and positive market presences.

First, the BOCs have now made or are making arrangements to recover the costs associated with the investment in complex inside wiring from the businesses who use the wire or from ratepayers as a whole. To reassign

this physical asset to AT&T after divestiture would alter the BOCs' revenue requirements, disrupt their rate schedules, and require fundamental changes in their marketing efforts. It would further require reassignments of some personnel who maintain or service this wiring from the BOCs to AT&T, thereby disrupting operations, working relationships, and employee morale within each BOC, and within AT&T as well.

Similarly, AT&T's operations would be profoundly disrupted by a post-divestiture decision to make it the owner of complex inside wiring. In addition to the effects on its employees, AT&T would be required to revamp its prices and marketing and maintenance operations to attempt to recover all or part of the Bell System's shareholders' investment in this physical asset. AT&T would thus find itself in the difficult position of having to develop charges to recover the costs of inside wiring that is used with the PBXs installed by its direct competitors in the CPE market, such as Rolm and Northern Telecom -- which could lead to the very type of post-divestiture controversies that the MFJ was intended to end. The adverse effects on the BOCs and AT&T would be exacerbated because the new arrangements would all have to be established on an emergency basis after divestiture.

B. Similarly, if California were to prevail after divestiture on its claim that Pacific's average cost of debt must be reduced, or the debt costs of all the BOCs' equalized, a mechanism would have to be developed to consolidate the

financial operations of the eight separately owned companies that will result from the reorganization, either by pooling all the outstanding debt issues of Bell System companies or by requiring ongoing payments among all companies. In either case, the companies would have to agree upon arrangements for the joint management of their debt portfolios, including such day-to-day financial decisions as whether and when to call debt issues before their maturity, whether to refinance these issues and, if so, with what new debt instruments. The necessary financial integration would exceed that under the Bell System's current operations, would divert critical managerial and operational resources from the tasks of establishing normal post-divestiture business operations, and would inject substantial uncertainty into the companies' finances, disrupting financial planning and investor decision-making at precisely the time it is most critical for the companies to establish investor confidence and unimpaired access to the capital markets.

C. More fundamentally, the provisions of the Plan are inextricably interrelated, not discrete as California and New York imply. A change in one part of the Plan can thus require changes in other parts of the Plan. For example, if the investment in complex inside wiring (or in the accounting entries for "station handling" in Account 232 that both California and New York raise) were reassigned to AT&T after divestiture, other changes would be required. The reassignment of this investment will obviously remove investment from the BOCs' books. California and New York could thus be expected to argue that AT&T would be required

to assume more of the BOCs' debt to assure that each had previously been divested with the MFJ-prescribed debt ratios -- as New York implicitly acknowledges in the last sentence of its jurisdictional statement (p. 8). But AT&T could contend that no additional debt need be assumed from some or all of the twenty-two BOCs, most of whom are being divested with lower than the MFJ-prescribed debt ratios, and, with or without owning the Account 232 investment, may still have been divested with the "approximately" 45% debt ratios (or 50% ratio in the case of Pacific) that Section VIII(H) of the MFJ requires. Similarly, if the Court decided for California on its claim that Pacific should have been divested with an average cost of debt of 9.2%, AT&T could contend on remand that no additional debt nonetheless need be assumed because AT&T has the right under the MFJ to increase Pacific's debt ratio from its present 46.5% to 50% -- which would more than offset the reduction in Pacific's annual total debt expense resulting from the decrease in the average cost of its debt.

Beyond the specific provisions of the Plan involved in this case, if significant changes in the Plan were ordered, the parties could reconsider other provisions of the Plan or of the MFJ, in order to preserve the balance achieved by the existing Plan. They would be free even to agree to modifications of the MFJ that would conform it to the construction that the parties and the District Court have given it in this case. In all events, it is certain there would be protracted proceedings in the District Court, a new round of objections and further appeals -- all of

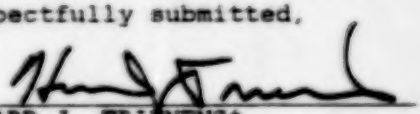
which would prolong the very interrelationship among the companies and the same crippling uncertainty that the entry and affirmance of the MFJ was supposed to end.

D. These considerations vividly demonstrate that the uncertainty that these appeals create will threaten national interests if the appeals are not finally resolved by January 1, 1984. Business and financial planning will be impeded for the Bell System companies, their competitors, and all telephone subscribers. The ensuing financial uncertainty will not only impair the trading of the stock of the to-be-established companies -- trading which the SEC permitted to begin on November 21, 1983 -- but, far more importantly, will seriously impair the ability of each of these companies to raise funds in capital markets during what will probably be the single most critical period in their future corporate existences: immediately after divestiture. These adverse consequences would be compounded by the possibility that marketing and operational arrangements could be disrupted during this critical period by post-divestiture decisions of these appeals.

9. The District Court and this Court have thus far taken all the necessary steps to assure that the uncertainty that the challenges to the reorganization create does not impair vital national industries and interests and therefore to prove that the federal judiciary can manage large antitrust cases. The only way to put a timely end to the potentially crippling uncertainty created by the two

final legal challenges to the reorganization is for this Court to decide these appeals now, before January 1, 1984.

Respectfully submitted,



HOWARD J. TRIENENS*
ALFRED A. GREEN
JIM G. KILPATRIC
FRANCINE J. BERRY
195 Broadway
New York, New York 10007
(212) 393-5111

GEORGE L. SAUNDERS, JR.
JOHN D. ZEGLIS
DAVID W. CARPENTER
DAVID D. HILLER
One First National Plaza
Chicago, Illinois 60603
(312) 853-7000

OF COUNSEL:

SIDLEY & AUSTIN

November 22, 1983

* Counsel of Record

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CLERK

Nos. 83-737 and 83-738

# In the Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, *Appellants*,

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE & TELEGRAPH COMPANY, ET AL., *Appellees*.

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE, *Appellant*,

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE & TELEGRAPH COMPANY, ET AL., *Appellees*.

**On Appeal from the United States District Court for the District of Columbia**

## MEMORANDUM IN SUPPORT OF JURISDICTIONAL STATEMENTS

James H. Bailey
General Counsel
Eddie M. Pope*
Assistant General Counsel
Oklahoma Corporation Commission
Room 460, Jim Thorpe Building
Oklahoma City, Oklahoma 73105
Telephone (405) 521-2255
*Attorneys for Appellees*

November, 1983

*Counsel of Record

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Nos. 83-737 and 83-738

In the
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THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,
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*Appellees.*

**On Appeal from the United States District Court for the District of Columbia**

# MEMORANDUM IN SUPPORT OF JURISDICTIONAL STATEMENTS

The Oklahoma Corporation Commission ("Oklahoma") is the regulatory agency with jurisdiction over rates and practices of telephone companies in Oklahoma. Oklahoma was a party below in *United States* v. *AT&T*, 552 F.Supp.

131 (D. D.C. 1982), *aff'd mem. sub. nom. Maryland* v. *United States*, ___ U.S. ___, 103 S.Ct. 1240, 75 L.Ed.2d 472 (1983). Pursuant to Rlue 10.4 of this Court, Oklahoma is an Appellee. Oklahoma supports the position of Appellants, People of the State of California ("California") and New York State Department of Public Service ("New York"). This Court should note probable jurisdiction in these cases and set them for plenary review.

Oklahoma adopts the Jurisdictional Statement of California for the description of the Opinions Below, Jurisdiction, Statutory Provisions and Statement of the Case.

## THE QUESTIONS ARE SUBSTANTIAL

As the District Court recognized, the AT&T divestiture is the "largest corporate reorganization in history" affecting "millions of employees and shareholders, the nation's telephone subscribers, AT&T's competitors, the telecommunications industry . . . and the responsibilities of federal and state regulatory bodies," App. at 353.

The immensity of this case is illuminated by the fact that the questions regarding station handling costs and complex inside wiring are not major issues in the case below — but represent over three *billion* dollars nationwide just for complex inside wiring, untold billion dollars for station handling costs; for Oklahoma, the investment represents $25 million for complex inside wiring and approximately $41 million for station handling costs. In any other case, these would be substantial numbers.

It is not just the numbers that make this case substantial.

The claimed error in this case is fundamentally one of disagreement over accounting. The experience of state telephone regulators was, in key respects, disregarded by a federal district court judge. Due to the press of time and certification in this case, this Court is the only forum in which the error can be corrected. This Court should allow the states a chance to present their case.

This case affects every telephone subscriber in America. It is a uniquely national case.

Understanding this case requires an understanding of some aspects of telephone engineering and accounting. These are fields coated with jargon. Oklahoma will try to cut through the complexity and present a simple explanation.

In the past, when you called the phone company for totally new phone service, the company would send a service agent who would string a wire from the nearest telephone pole to your home. In technical terms, this is the "drop wire" to the "protector". The protector is frequently on the outside of the residence and protects the phone system from damage from lightning. Then the service agent would wire the inside of the house from the protector to the service jack. This is "simple inside wiring". The service agent would install the telephone and test it. This is "station handling".

There are differences with business systems. If a business has several incoming lines or several telephones tied together with an intercom, it has "key system apparatus" or "private branch exchanges" ("PBXs"). Wiring these telephones together is more difficult and requires more time

of the service agent than residential-type wiring. It is called "complex intrasystem wiring".

In the past, the costs of all these "station connections", both residential and business, was accounted for in Account 232 of the FCC's Uniform System of Accounts. They were "capitalized", that is, treated as long-term investments on which the telephone companies earned a rate of return. This long-term recovery of these costs was chosen so as to keep as low as possible the initial cost of hooking up to the system. This encouraged widespread installation of telephones for everyone, or "universal service."

This long-term recovery caused problems because the sum of these station connections continued to grow. In 1979, the Bell system installed approximately 36 million telephones and removed approximately 31 million telephones, *Amendment of Uniform System of Accounts*, 85 F.C.C.2d 818, 824 (1981). All of the costs of these changes, including the labor charges, were booked to Account 232.

The FCC recognized this enormous capital outlay was a burden to the system. In 1981, it ordered all future inside wiring to be "expensed", that is, treated as an operating expense which allows for a far more rapid recovery of the costs. (The drop wire and protector continued to be capitalized.) The FCC authorized the accumulated inside station connection and inside wiring investment to be recovered over a ten-year amortization period.

In 1980, the FCC moved to deregulate "customer premises equipment" (CPE), which includes telephones, PBXs and key units. In the first order the Commission excluded inside wiring from the definition of CPE, *Amendment of*

*Section 64.702 of The Commission's Rules and Regulations (Second Computer Inquiry)* Docket No. 20828, 77 F.C.C.2d 384, 447, 35 P.U.R.4th 143, 205 n.57 (1980). In a subsequent order, the FCC stated that the issue of inside wiring "was not addressed" in earlier proceedings, and was specifically reserved for a later proceeding, 84 F.C.C.2d 50, 69, 39 P.U.R.4th 319, 341 (1980).

On January 8, 1982, the parties in the AT&T antitrust case filed a stipulated "Modification of Final Judgment". On August 11, 1982, Judge Greene filed his opinion in that case (App. 1-172), and the companion Modification of Final Judgment was filed August 24, 1982 (App. 173-190). The Modification of Final Judgment assigned to AT&T "all facilities, personnel and books of account . . . relating to . . . the provision of customer premises equipment to the public." (MFJ, §§I(A)(2), I(A)(4); App. at 174-175.) "Customer premises equipment" was defined as "equipment employed on the premises of a person . . . to originate, route or terminate telecommunications," not including "equipment used to multiplex, maintain or terminate access lines." (MFJ, §IV(E); App. at 177.)

On December 16, 1982, AT&T filed a Proposed Plan of Reorganization. That plan assigned all of the customer premises equipment to AT&T, but all of the embedded cost of installing that equipment (Account 232) to the proposed new regional Bell Operating Companies (BOCs). Several state commissions and the National Association of Regulatory Utility Commissioners protested the assignment of the inside wiring and station handling costs to the BOCs.

On February 28, 1983, this Court affirmed the Modified Final Judgment, *Maryland* v. *United States*, ___ U.S. ___,

103 S.Ct. 1240, 75 L.Ed.2d 472 (1983). The treatment of the issues relating to station connections were still being litigated. On March 14, 1983, AT&T filed its "Response to Objections to its Proposed Plan of Reorganization". It claimed there was "no way" to determine station handling costs (p. 154) and claimed "no distinction" could be made for complex inside wiring (pp. 154-155). Even AT&T noted, however, that New York was already charging separate charges for inside wire (p. 163, n.**).

State commissions protested that the various elements of Account 232 *could be* and *had been* segregated (Comments, N.Y. Dept. Pub. Serv. at 11; Further Comments, Calif. Pub. Util. Com'n at 24; Reply Comments, CPUC, at 26).

The District Court conditionally approved the Plan of Reorganization on July 8, 1983 (App. 195-330). There was *no* mention of the complex intrasystem wiring and station handling claims. On July 28, 1983, the District Court dealt with an AT&T Motion for Partial Reconsideration. It dismissed Account 232 claims along with "patent licensing" claims in a footnote (App. at 339, n.18).

The modified Plan of Reorganization was approved by the District Court on August 5, 1983. In the memorandum approving the Plan, the court described AT&T ownership of inside wiring as creating a "bottle-neck". The court was persuaded by AT&T that "there is no practical way to separate" the various costs (App. at 344). The District Court did acknowledge that "a theoretical case could be made" that some portion of Account 232 should follow the embedded customer's premises equipment.

The case is more than theoretical. The states had demonstrated that AT&T's costs *could* be separated in a reasonable manner. The District Court should have deferred to the experience of the state regulatory agencies, and conditioned approval of the Plan on the appropriate allocation of these costs to AT&T.

District courts should have a "scrupulous regard" for state public service commissions, *Alabama Public Service Com'n* v. *Southern Railway Co.*, 341 U.S. 341, 349 (1951). The ratemaking process is "essentially empiric. The stuff of the process is fluid and changing . . ." *Board of Trade* v. *United States*, 314 U.S. 534, 546 (1942). It is not an area well suited for court determination. The District Court should have granted great deference to the experience of state regulators. If state regulators say an account can be meaningfully divided, the courts should recognize that it probably can be divided. This Court has recognized that such disputes are:

> for the regulatory commission and not for the courts. We repeat that for a court to upset an accounting order it must be 'so entirely at odds with fundamental principles of correct accounting' . . . as to be the expression of a whim rather than an exercise of judgment. — *United States* v. *New York Telephone*, 326 U.S. 638, 655 (1946)

The state regulatory commissions have established reasonable accounting distinctions for separation of Account 232. The Federal Communications Commission has detariffed intrasystem wiring installed in the future, *In the Matter of Modifications to the Uniform System of Accounts for Class A and Class B Telephone Companies*, CC Docket No.

82-681, Order November 2, 1983. The regulatory judgment is that the purchaser of the customer premises equipment should pay for the costs of installing that equipment. The District Court erred in placing the equipment with AT&T, and the installation costs with the Bell Operating Companies.

The District Court contradicted its own prior order. The District Court should have recognized that station handling and complex intrasystem wiring were part of the "books of account . . . relating to . . . the provision of customer premises equipment to the public" (MFJ, §§I(A)(2), I(A)(4); App. at 174-175). The District Court should have corrected AT&T when it assigned some accounts of the wiring used "to originate, route and terminate telecommunications" (MFJ, §IV(E); App. at 177) to the Bell Operating Companies.

## CONCLUSION

The District Court contradicted the judgment of experienced state regulatory commissions. The District Court contradicted equitable principles that the person receiving the benefit (*i.e.*, CPE) should pay the costs associated with that benefit. If this Court does not correct the contradictions, every telephone ratepayer in America will be required to pay their local Bell companies for the accrued cost of installing equipment that AT&T now owns. This Court is now the only chance to rectify that error. This Court should note probable jurisdiction in the appeals filed by California and New York.

Respectfully submitted,

JAMES H. BAILEY
General Counsel

EDDIE M. POPE*
Assistant General Counsel
Oklahoma Corporation Commission
Room 460, Jim Thorpe Building
Oklahoma City, Oklahoma 73105
Telephone (405) 521-2255

*Attorneys for Appellees*

*Counsel of Record

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No. 83-737

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA & THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

vs.

UNITED STATES OF AMERICA, *et al.*,

*Appellees.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

## MOTION TO AFFIRM OF APPELLEE PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA

Lloyd N. Moore, Jr.
*Counsel of Record*
for Appellee, Public Service Commission of the District of Columbia
Geltner & Newsom
Number Ten E Street, S.E.
Washington, D.C. 20003
Tele: (202) 547-1136

Roberta Willis Sims
*Acting General Counsel*
Public Service Commission of the District of Columbia
451 Indiana Avenue, N.W.
Washington, D.C. 20001
Tele: (202) 727-3050

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necessary that he make a public interest determination on the proposed MFJ, J.A. 148-149, but that the Tunney Act required that he retain jurisdiction and insist, as a condition of approval of the MFJ, that it be amended to also require the Court's approval of the plan of reorganization. J.A. 156. As a result, Judge Greene decided to make the Tunney Act decision in two stages; first he would decide whether the MFJ was in the public interest, and, second, he would decide if the plan of reorganization conformed to his initial determinations so as to likewise be in the public interest.

In his August 12, 1982 order, Judge Green examined the issue of debt distribution as part of his overall consideration of the division of assets and liabilities.[3] J.A. 133-138. Questions were raised as to the appropriate debt-equity ratios, and Judge Greene accepted the suggestions of A.T.&T. and the Department of Justice that A.T.&T. divest the BOCs with debt-equity ratios of approximately 45% and assume its representative share of outstanding debt. Judge Greene interpreted his Tunney Act duties to require that the debt distribution proposal be made a part of the MFJ, so he would be in a position, if necessary, to insist that the statements of intention were actually implemented. J.A. 137.

As part of his consideration of the debt issue, Judge Greene pointed out that Pacific's debt-equity ratio was around 75%, substantially higher than the Bell System

[3]Given the fact that 22 BOCs were being separated from the Bell System and the fact that the Bell System had been highly integrated, the intervenor parties and Judge Greene were concerned about both the multiplicity of decisions to be made and the risk that the parent would manipulate the division of assets and liabilities to its benefit and the BOCs' detriment.

tion of the public interest determination which was required by the Tunney Act. As a result, this Court's role in this appeal is to review the public interest determination. The only case discussing the scope of an appellate court review of a Tunney Act public interest determination suggest that the appellate court's role is extremely limited; it is primarily to assure itself that the district court applied the proper Tunney Act standard and procedures. See *United States v. Bechtel,* 648 F.2d 660 (9th Cir. 1981). Once the District Court has applied the proper standard and has followed required procedures, its decision to approve a settlement under the Tunney Act is essentially discretionary; there is nothing in the reported decisions or the Tunney Act's legislative history to suggest tht the reviewing court's standard is other than the abuse of discretion standard normally applied in such situations.[6]

### B. California's Lack of Equity

The cost of debt that the plan of reorganization provides for Pacific is entirely proper under the circumstances of the case. The objections of California to that cost of debt lack merit, and, therefore, this Court should summarily affirm the decision of the District Court to divest

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[6] *United States v. Bechtel, supra* is the only reported court of appeals decision reviewing a Tunney Act public interest determination. There are numerous district court decisions in addition to Judge Greene's August 12, 1982 opinion, J.A. 26-36 which examine the standard to be applied by a district court in deciding whether to accept a settlement. See, e.g., *United States v. Carrols Dev.Co.,* 454 F. Supp. 1215, 1222 (N.D.N.Y. 1978); *United States v. National Broadcasting Co.,* 449 F. Supp. 1127, 1143 (D.D. Cal. 1978); *United States v. Gillette Co.,* 406 F. Supp. 713, 716 (D. Mass. 1975). The legislative history of the Tunney Act is at 1974 U.S.Cong. Code & Admin. News 6535 (HR 93-1463).

Pacific with an average cost of funded debt of approximately 9.5%.

At least two reasons, having to do with economic growth and utility regulatory policy in California, justify the decision of the District Court. First, California, like the rest of the Sunbelt, has experienced a faster rate of growth than have other parts of the Country. Plan at 194-195. That faster growth rate has caused greater utility plant construction. As a consequence, BOCs in the Sunbelt, like Pacific, have issued debt more recently and more frequently than have BOCs serving slower growth areas. Since the cost of debt has risen in recent years, the average cost of debt of the Sunbelt BOCs has been higher than that of other BOCs. *Id.* California concedes that Pacific has had significant capital needs recently and that the lack of equity investment in Pacific has meant massive high cost debt. California Preliminary Comments at 23.

Second, there is considerable evidence in the record to show that utility regulatory policies in California may have led to higher costs of debt for Pacific than even for other Sunbelt BOCs, much less non-Sunbelt BOCs. See A.T.&T. Response at 285-298. California maintains that AT&T has refused to invest equity in Pacific, California Preliminary Comments at 15, but has not explained just why this is so. And AT&T has referred to a planned equity offering in 1979 of 10,000,000 shares of Pacific that the BOC aborted on the advice of the BOC's investment bankers because its earnings record made the offering impossible on reasonable terms. AT&T Response at 291-292. California has not replied to this point.

Thus it has come to pass that the cost of debt varies among the BOCs, with Pacific having the highest such cost. The District Court clearly recognized that this might be the case when it stated that

> The Court expects that the plan of reorganization will provide each Operating Company with a debt portfolio that reflects the terms and conditions comparable to the debt held by the Bell System as a whole unless it can be shown that, with respect to a particular Operating Company, its own current debt provides a more equitable basis.

(J.A. 137 n.321)

Furthermore, Section VIII(H) of the MFJ provides that equalization of debt costs may yield to exceptions. J.A. 185. The basis for an exception, of course, would be that the equities warrant the grant of an exception. See J.A. 137 n.321. It is abundantly clear that the equities militate against California's request for a 9.2% cost of debt. Rather, quite to the contrary, they point to a higher cost of debt for Pacific than for other BOCs.

The fundamental problem is that to grant California's request will mean that someone else will have to bear the expense represented by the difference between servicing debt at a cost of 9.2% and servicing it at a cost of 9.5%. The question is who that someone else is. California says that spreading Pacific's high debt cost does not have to "significantly disadvantage" any BOC and that the burden of Pacific's debt can fall "primarily" on AT&T. California Preliminary Comments at 25. California later claimed that matters can be arranged so that AT&T alone would bear the burden of reducing Pacific's debt cost. California Reply Comments at 9.

It is not clear that the other BOCs can be insulated from the adverse effects that would result from spreading Pacific's high cost of debt. If AT&T's costs must increase in order to satisfy California's demand for lower debt cost, it

may well be that ratepayers in the District of Columbia and elsewhere will have to pay higher rates to AT&T.

Furthermore, California first represented to the District Court that the other BOCs would in fact suffer some disadvantage. California Preliminary Comments at 25. Leaving aside the problems of which representation to believe, it seems altogether probable that AT&T would not feel bound to shoulder the entire burden by itself and would therefore share the burden with other BOCs or that the district court, on a remand, would effect such a result.

California has claimed, in effect, that Pacific's high debt cost is AT&T's fault. It has not proved that allegation[7] and it has not established, therefore, any reason why AT&T should not be allowed to place some or all of the burden that California wishes to impose on AT&T on other BOCs.

California has failed to demonstrate that other BOCs and their ratepayers must suffer the consequences of Pacific's high cost of debt. Nothing in the record in this case remotely suggests that ratepayers in the District of Columbia or the BOC there, for exmaple, are responsible for the differential in the rates of economic development in California and the Sunbelt on the one hand and growth in other parts of the country. Nothing in the record supports the notion that District of Columbia ratepayers or the BOC that serves them drove equity investors away from Pacific.

The District Court quite correctly and properly concluded that low growth areas of the country should not subsidize high growth areas. J.A. 221-222 n.64. Furthermore,

[7]If anything, AT&T has proved the contrary. See AT&T Response at 285-298.

while the District Court retreated somewhat from the conclusion that California regulators drove up Pacific's cost of debt, compare J.A. 137 n.320 to J.A. 221 n.64, the fact remains that the record shows that the investment community so believed, see AT&T Response at 285-298, and, therefore, the impact of Pacific's cost of debt was the same that would have resulted if the California regulators had forced up that cost. At the very least, California failed to dispel the supposed misimpression concerning its regulatory policies affecting Pacific.

Furthermore, California has already managed to get AT&T to agree to a 46.5% debt-equity ratio rather than the 50% ratio earlier authorized by the District Court, see J.A. 137 n.320, J.A. 184, and an average cost of funded debt of 9.5%, which is apparently lower than actual pre-divestiture cost. See California Reply Comments at 7-8. The effect of these concessions is necessarily to shift the burden of some of Pacific's high costs elsewhere. Yet no one has complained of that fact. California's desire for even more, under the circumstances, should not be satisfied.

Finally, it appears that Southwestern Bell's cost of debt has increased from 9.1% to 9.4%. See Plan at 194; AT&T Motion to Affirm at 22. Thus California is seeking a lower cost of debt than that that Southwestern Bell will have to carry, even though no one has complained in this proceeding about the policies of those who have regulated Southwestern Bell over the past few years or about that BOC's cost of debt. There is nothing in the record that can support a further reduction in Pacific's cost of debt from 9.5% to 9.2% in the face of Southwestern Bell's current cost of 9.4%.

The equities line up solidly against California. California has not shown that Pacific's cost of debt is the fault of

## QUESTION PRESENTED

Whether the District Court violated the Tunney Act, 15 U.S.C. §16, when, after approval of the settlement of the A.T.&T. antitrust case, the District Court approved the plan of reorganization of the Bell System without requiring that the average cost of long-term funded debt retained by Pacific Telephone & Telegraph Company ("Pacific") be reduced to the average of the Bell system.

The D.C. Commission regulates local telephone rates and services in the District of Columbia. As such, it has jurisdiction over The Chesapeake & Potomac Telephone Company, which is presently a Bell System operating company ("BOC"). The D.C. Commission was a party below and, pursuant to Rule 10.4, is an appellee in this appeal. Its primary interest in this appeal is brought about by the possibility that part of Pacific's high cost debt will be distributed to other BOCs and, as a result, burden local ratepayers in the District of Columbia. For that reason, it is interested in the second question presented in the jurisdictional statement filed by the People of the State of California and the Public Utilities Commission of California (collectively referred to as "California"). The D.C. Commission moves the Court to affirm as to that issue.[1]

## STATEMENT OF THE CASE

Following the parties' settlement agreement in *United States v. American Telephone & Telegraph Co.*, Judge Greene, who was presiding over that case, ruled that he would follow the Tunney Act, 15 U.S.C. §16, in deciding whether to accept the settlement. J.A. 25.[2] There were ex-

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[1]The D.C. Commission takes no position regarding the first issue, which is presented by both California and by the appellant in No. 83-738.

[2]Judge Greene never flatly ruled that he was required to follow the Tunney Act. See J.A. 19-22, 25 n.66. The parties, however, acquiesced in Judge Greene's following the Tunney Act, J.A. 22, and, in the appeals from his August 24, 1983 modification of final judgment ("MFJ") no party contended that Judge Greene had erred in following the Tunney Act. As a result, the applicability of the Tunney Act is the law of the case. It should be noted, however, that, although Judge Greene did not technically rule that the Tunney Act had to be followed, he made clear his view that it had to apply and that a public interest determination had to be made. J.A. 20-21.

tensive Tunney Act proceedings, after which Judge Greene entered an order on August 12, 1982, J.A. 1, ruling that, in the event the parties made certain significant changes in the settlement agreement, he would approve the settlement. The settlement agreement actually involved a dismissal of the then-pending government antitrust charges in *United States v. American Telephone & Telegraph Co.*, D.D.C. C.A. No. 74-1698, and a modification of the final judgment in *United States v. Western Electric Co.*, D.D.C. C.A. No. 82-0192. In the latter case, there had been a 1956 consent decree in a government antitrust case commenced in 1949 which, as part of the 1982 settlement review procedures, was transferred to the District of Columbia for consolidation. Judge Greene's required changes dictated amendments of the modification of the final judgment ("MFJ") in *Western Electric* to which the parties had agreed.

In view of the magnitude of the case and the numerous issues presented by the settlement, Judge Greene was faced with varous alternatives as to how and when to make the public interest determination contemplated by the Tunney Act. Under the settlement agreement, the government and A.T.&T. contemplated entry of an MFJ to be followed six months later by A.T.&T.'s filing of a detailed plan of reorganization for Department of Justice review. The Department of Justice and A.T.&T. viewed the Court's role as limited to review of the MFJ, leaving approval of the plan of reorganization to the Department of Justice. Many of the intervenor parties, however, argued that it was impossible to make a proper Tunney Act public interest determination without the plan of reorganization before the Court and that Judge Greene should defer final approval until he had the plan of reorganization before him. J.A. 147-148. Judge Greene concluded that it was

average, due to actions of California's regulators. J.A. 1378 n.320. Judge Greene ruled that he would accept a reduction of Pacific's debt to 50%. *Id.* He then added, as a required modification, the following provision:

> H. At the time of the transfer of ownership provided for in section I(A)(4), the separated BOCs shall have debt ratios of approximately forty-five percent (except for Pacific Telephone and Telegraph Company which shall have a debt ratio of approximately fifty percent), and the quality of the debt shall be representative of the average terms and conditions of the consolidated debt held by A.T.&T., its affiliates and the BOCs at that time. Upon application by a party or a BOC, the Court may grant an exception to this requirement.

The parties accepted the required changes in the MFJ and, as a result, Judge Greene entered the MFJ on August 24, 1982. There were several appeals. After Judge Greene certified them to this Court under the Antitrust Expediting Act, 15 U.S.C. §29, the Court summarily affirmed on February 22, 1983. *Maryland v. United States,* ___ U.S. ___, 103 S.Ct. 1240 (1983). One of the issues raised in the appeal was the validity of the public interest standard which Judge Green had applied. The Court wrote no opinion, but it is clear that the matter was before the Court and considered, because it is discussed in the opinion of three Justices dissenting from summary affirmance. No appellant complained about Judge Geene's decision to continue the public interest determination process into a review of the plan of reorganization or the substantive decision to approve the proposed debt-equity ratio but to make it part of the MFJ.

In the meantime, approval of the plan of reorganization was conducted in two stages; Judge Greene would first ex-

amine the reconfiguration of the long distance network[4] and then review the division of assets and liabilities. J.A. 195. In both instances, he used the same decisional mechanism; he indicated what changes he would require of the parties as a prerequisite to his approval of the relevant portion of the plan of reorganization.

In his July 8, 1983 order setting out the changes that he would require in the plan of reorganization, Judge Greene demanded significant changes in such important matters as ownership of trademarks and patent licensing because of his analysis of the public interest. California complained about the part of the plan of reorganization which distributed debt to Pacific, arguing that Pacific should not be given long term debt which had a higher cost of servicing than the Bell System average. Judge Green rejected this claim together with several others relating to liabilities and debt, but he did not specifically discuss his analysis of California's claim. J.A. 221, n.64.

## SUMMARY AFFIRMANCE

### A. The Legal Standard

Under the Antitrust Expediting Act, 15 U.S.C. §29, this Court's role is essentially the same as that which a court of appeals would have served if the district court had not certified direct appeal.[5] As indicated earlier, Judge Greene's review of the plan of reorganization was really a continua-

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[4]Order of April 20, 1983, not included in J.A.

[5]See *United States v. duPont deNemours & Co.*, 366 U.S. 316, 321-325 (1961); *Int'l. Boxing Club v. United States*, 358 U.S. 242, 253 (1959).

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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1983

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No. 83-737

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THE PEOPLE OF THE STATE OF CALIFORNIA & THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

*Appellants,*

vs.

UNITED STATES OF AMERICA, *et al.*,

*Appellees.*

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

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## MOTION TO AFFIRM OF APPELLEE PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA

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### MOTION TO AFFIRM

Appellee Public Service Commission of the District of Columbia ("the D.C. Commission") moves the Court pursuant to Rule 16(c) to affirm the judgment sought to be reviewed on appeal on the ground that it is manifest that the question on which the decision of the cause depends is so insubstantial as not to need further argument.

AT&T. Therefore, neither AT&T nor any of the other BOCs should be asked to take on any more of Pacific's costs than AT&T has previously agreed to do. In addition, the actions taken by AT&T to date regarding Pacific's debt-equity ratio and debt cost have markedly enhanced Pacific's future prospects. See J.A. 221-222 n.64. No credible basis exists, therefore, for the further relief sought by California.

## CONCLUSION

The Court should summarily affirm.

Respectfully Submitted,

Lloyd N. Moore, Jr.
*Counsel of Record*
for Appellee Public Service Commission of the District of Columbia
Geltner & Newsom
Number Ten E Street, S.E.
Washington, D.C. 20003
Tele: (202) 547-1136

Roberta Willis Sims
*Acting General Counsel*
Public Service Commission of the District of Columbia
451 Indiana Avenue, N.W.
Washington, D.C. 20001
Tele: (202) 727-3050

December 7, 1983